

collect, verify, and retain the required information, and to provide the required notice to customers. The cost-benefit analysis in the proposed rule did not discuss the time and costs associated with computer system modifications, but commenters suggested that these costs could be substantial. The Commission estimates, based on discussions with industry representatives, that it will cost each fund or fund family approximately \$40,000 to make these types of system modifications.¹³² Therefore the Commission estimates that there will be a one-time aggregate cost of approximately \$36 million for these systems modifications.

2. Ongoing Costs

As mentioned above, ongoing costs for mutual funds will be associated with the need to: (1) Collect the information required by the CIPs, (2) verify customers' identities, (3) determine whether customers appear on lists provided by federal agencies, and (4) make and maintain records related to CIPs.

Information Collection. Although mutual funds generally require customers to provide a name and mailing address in order to open an account, mutual funds currently may not require all fund customers to provide all of the information required to be collected pursuant to a CIP. Moreover, mutual funds may not be collecting all such information with respect to all of the persons who will be considered to be customers for purposes of the new rule. Therefore the Commission anticipates that mutual funds will incur costs in connection with the collection of identifying information from their customers. Based on discussions with industry participants, the staff of the SEC estimates that the average time spent collecting the required information will be between one and four minutes per account and that the hourly personnel

and overhead cost associated with these requirements will be \$25 per hour. Therefore, the SEC staff estimates that this burden will result in an aggregate annual cost to the industry of between \$6.7 million and \$26.7 million.¹³³

Information Verification. The new rule also requires CIPs to contain procedures for funds to verify customer identities. The rule provides funds with substantial flexibility to decide how they will verify identification information. The purpose of making the rule flexible is to give funds the ability to select verification methods that are, as section 326 requires, reasonable and practicable. The new rule allows a mutual fund to employ such verification methods as permit it to form a reasonable belief that it knows the true identities of its customers.

The rule sets forth non-exclusive lists of methods that a fund may use to verify customer identification. A fund may use other reasonable methods that are currently available, or that become available in the future. The Commission believes that verifying the identifying information could result in costs for mutual funds because some firms currently may not use verification methods. Based on discussions with industry participants, the SEC staff estimates that the total annual cost to the industry to verify the identifying information will be between \$49.3 million and \$98.6 million.¹³⁴

Resolution of discrepancies. Based on discussions with industry participants, the staff of the SEC believes that initial detection of discrepancies in information collected will be automated and conducted on a batch-file basis. Once discrepancies have been detected, staff of the SEC estimates that the average time spent by compliance personnel to resolve discrepancies in information collected will be between one and four minutes per account and that the hourly personnel and overhead

cost associated with these requirements will be \$25 per hour. Therefore, the SEC staff estimates that this burden will result in an aggregate annual cost to the industry of between \$6.7 million and \$26.7 million.

Comparison with government lists of known or suspected terrorists. Section 326 and the new rule require that mutual fund CIPs include reasonable procedures for determining whether a customer's name appears on designated lists of known or suspected terrorists or terrorist organizations issued by any federal government agency. Mutual funds should already have procedures for determining whether customers' names appear on some federal government lists. There are substantive legal requirements associated with the lists circulated by Treasury's Office of Foreign Asset Control (OFAC). Failure to comply with these requirements may result in criminal and civil penalties. Based on discussions with industry representatives the SEC staff estimates that the annual cost to the mutual fund industry of this requirement will be \$3.4 million.¹³⁵

Recordkeeping. The Commission believes that the recordkeeping requirement in the new rule will result in additional costs for mutual funds that currently do not maintain certain of the records for the prescribed time period. We believe that most funds already retain certain of the records required by the new rule as a matter of good business practice.

The proposed rule provided that mutual fund CIPs provide for the retention of all information for five years after a customer account is closed. The final rule bifurcates the record retention provisions so that funds will be required to retain customer identification information for five years after the account is closed, and to retain a description of (1) the documents relied upon to verify the customer's identity, (2) the methods and results of measures undertaken to verify the identity a customer and (3) the resolution of any substantive discrepancies discovered during the identity verification process for five years after the date the record was made. The SEC staff estimates, based on discussions with

¹³² Based on discussions with industry representatives, SEC staff estimates that it will take compliance personnel fifteen hours, at \$62 per hour (\$930) to modify fund account applications in order to collect all of the required information from and provide required notice to fund customers. The SEC staff estimates that the aggregate cost of such modifications will be approximately \$828,000 (\$930 per fund family × 890 fund families). Based on discussions with industry representatives, the SEC staff estimates that it will take computer programmers 640 hours at \$62 per hour to implement the necessary computer system modifications (\$39,680). The SEC staff estimates the aggregate cost of these modifications to be \$35.3 million (\$39,680 per fund family × 890 fund families). Thus, the SEC staff estimates the total costs of systems modifications to be \$36.1 million (\$35.3 million + \$828,000).

¹³³ We estimate that there are 16 million new mutual fund shareholder accounts created each year. Therefore, we estimate the range of cost to be between \$6.7 million (16 million new accounts per year × $\frac{1}{60}$ of an hour × \$25) and \$26.7 million (16 million new accounts per year × $\frac{1}{15}$ of an hour × \$25).

¹³⁴ The SEC staff believes that the processing costs associated with verification methods will be between \$1.00 and \$2.00 per account. The SEC staff further estimates that the average time spent verifying an account will be between five and ten minutes. The hourly cost of the person who would undertake the verification is estimated to be \$25 per hour including overhead. Therefore, the estimated costs to the industry reported above are between: \$49.3 million ((16 million new accounts per year) × (\$1.00) + (16 million new accounts per year) × ($\frac{1}{12}$ of an hour) × (\$25)) and \$98.6 million ((16 million new accounts per year) × (\$2.00) + (16 million new accounts per year) × ($\frac{1}{6}$ of an hour) × (\$25)).

¹³⁵ Based on discussions with industry representatives, the SEC staff estimates that it takes a data entry clerk approximately 30 seconds to ascertain whether a customer's name is on a government list. We assume that for most mutual fund customers this check will be automated and conducted on a batch-file basis. Therefore we estimate that cost of this requirement is \$.21 per customer ($\frac{1}{120}$ hour × \$25 per hour (cost per hour of data entry)). We estimate the aggregate annual cost of this requirement to be \$3.4 million (\$.21 per customer × 16 million customers).