This FAQ is based on current information and is not intended to be a comprehensive treatment of each issue an adviser may need to address. It is not a substitute for legal advice. The IAA undertakes no responsibility to update this FAQ.

INVESTMENT ADVISER ASSOCIATION

**Frequently Asked Questions*
Regarding Regulation S-P Disposal Rule[1]**

June 2, 2005

In December 2004, the Securities and Exchange Commission adopted amendments to Regulation S-P requiring all registered investment advisers to properly dispose of "consumer report information," maintained or possessed for a business purpose, by taking reasonable measures to protect against unauthorized access to or use of the information in connection with its disposal (the "disposal rule").[2] Reasonable disposal measures include adopting disposal rule policies and procedures which may be incorporated into an adviser's existing safeguard rule policies and procedures under Regulation S-P. All investment advisers will need to review their privacy policies and procedures to ensure compliance with the SEC's new rule. Each firm should consider how to tailor the policies and procedures to its unique business. Advisers are required to be in compliance with the new disposal rule by July 1, 2005, with one exception described below.

In addition to adopting the disposal rule, the SEC also amended Regulation S-P to require by July 1, 2005 that advisers' safeguard rule policies and procedures be in writing.[3]

The following Questions and Answers may help advisers implement and comply with the disposal rule's requirements.

Generally

Q1: Why did the SEC adopt rules requiring proper disposal of consumer report information?

A1: Congress passed the Fair and Accurate Transactions Act of 2003 (FACT Act), which amended the Fair Credit Reporting Act (FCRA) (15 U.S.C. § 1681w). Pursuant to the amended FCRA, the SEC adopted rules requiring that registered investment advisers, investment companies, brokers and dealers (other than notice-registered broker-dealers), and registered transfer agents that maintain or otherwise possess for a business purpose consumer report information, or any

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* The updated IAA Compliance Control regarding privacy and the Regulation S-P disposal rule may be obtained by IAA members by contacting the IAA directly.

1 *Final Rule: Disposal of Consumer Report Information*; SEC Rel. No. IA-2332 (Dec. 2, 2004) (also referred to as "rule" and "release"). The rule may be accessed at http://www.sec.gov/rules/final/34-50781.htm.

2 *See* 17 C.F.R. § 248.30(b).

3 *See* 17 C.F.R. § 248.30(a).

compilation of consumer report information derived from consumer reports, to properly dispose of the information or compilation. The rules are intended to protect consumers against unauthorized access to information about them that is contained in their consumer report and to protect against identity theft and fraud.

Q2: Under what circumstances would the disposal rule apply to an adviser?
A2: Advisers that maintain or otherwise possess "consumer report information" for a business purpose are subject to the rule.

Consumer Report Information

Q3: What does "consumer report information" mean?
A3: "Consumer report information" is defined to mean any record about an individual, whether in paper, electronic or other form, that is a consumer report or is derived from a consumer report. Consumer report information also means a compilation of such records.

Q4: Does the term "consumer report information" include aggregate information or blind data about consumers that does not identify an individual?
A4: No. Information that does not identify an individual is not covered by the definition of "consumer report information." *See also* Q7.

Q5: What is a "consumer report"?
A5: "Consumer report" under the disposal rule has the same meaning as in Section 603(d) of the FCRA (15 U.S.C. § 1681a(d)), which defines it as any written or other communication of any information *by a consumer reporting agency* (defined in 15 U.S.C. § 1681a(f)) bearing on a consumer's credit worthiness, credit standing, credit capacity, character, general reputation, personal characteristics, or mode of living which is used or expected to be used or collected in whole or in part for the purpose of serving as a factor in establishing the consumer's eligibility for: (1) credit or insurance to be used primarily for personal, family, or household purposes; (2) employment purposes; or (3) any other permissible purpose authorized under Section 604 of the FCRA (15 U.S.C. § 1681b).

Under Section 604, a consumer reporting agency may furnish a consumer report only under the following circumstances: (1) in response to a court order; (2) in accordance with the consumer's written instructions; (3) to a person the consumer reporting agency believes: (i) intends to use the information for a credit transaction involving the consumer and an extension of credit or collection of account, (ii) intends to use it for employment purposes, (iii) intends to use it for underwriting the consumer's insurance, (iv) intends to use it in connection with a determination of the consumer's eligibility for a government license to consider the person's financial responsibility or status, intends to use it, as a potential investor or servicer, or current insurer, in connection with the valuation or assessment of the consumer's credit or prepayment risks, or (v) has a legitimate

business need for the information in connection with a business transaction initiated by the consumer or in connection with reviewing an account to determine whether the consumer continues to meet the terms of the account; (4) in response to a request from a governmental child support agency; or (5) to a state agency to set a child support award.

Q6: What is excluded from the definition of "consumer report"?

A6: A consumer report does *not* include any (1) report containing information solely as to transactions or experiences between the consumer and the person making the report; (2) communication of that information among persons related by common ownership or affiliated by corporate control; or (3) communication of other information among persons related by common ownership or affiliated by corporate control, if it is clearly and conspicuously disclosed to the consumer that the information may be communicated among such persons and the consumer is given the opportunity, before the time that the information is initially communicated, to direct that such information not be communicated among such persons.

Q7: When would an adviser possess "consumer report information"?

A7: An adviser that obtains a consumer report for a business purpose will be considered to be in possession of consumer report information. For example, some advisers may possess consumer report information by obtaining a client's consumer report in connection with providing financial planning services. Others may obtain a consumer report in connection with making an employment decision about an individual. In addition, advisers would possess consumer report information if they obtain an individual's consumer report for anti-money laundering compliance purposes.

In addition, the SEC indicated that *any information derived from a consumer report that identifies an individual*, including a person's name and a variety of other identifiers, would bring that information within the scope of the rule. These identifiers include, but are not limited to, a social security number, phone number, physical address, and e-mail address. Therefore, this information is also governed by the rule. The SEC did not include a rigid definition of consumer report information in the disposal rule because, depending on the circumstances, items of information that are not inherently identifying can, in combination, identify particular individuals.

Q8: Some consumer report information, such as an individual's bankruptcy history, may be publicly available. Does the rule govern disposal of consumer report information that may be publicly available?

A8: Yes. The definition of consumer report information includes information that is included in a consumer report, whether it is public or not.

Q9: How do "customer" records and information covered under Regulation S-P's safeguard rule differ from "consumer report information" covered under Regulation S-P's disposal rule?

A9: These terms refer to two different, but potentially overlapping, sets of information. "Customers" are "consumers" (natural persons who obtain or have obtained any financial product or service from a financial institution that is to be used primarily for personal, family or household purposes) who have a continuing relationship with a financial institution. "Consumer report information" may be both broader and narrower than "customer records and information" – broader because it may include employees, not only clients, and narrower because it is derived from a consumer report rather than received from the client himself.

Q10: How should an adviser assess whether it has consumer report information?

A10: An adviser should assess its business practices to determine where it obtains information about individual clients, potential clients and/or potential or current employees. If an adviser obtains consumer reports on these individuals for business purposes, the adviser should identify the exact use and chain of control of the report, as well as the use of the information from the report.

Q11: Does the rule govern an adviser's use of its affiliate's consumer report information?

A11: It depends. A "consumer report" does *not* include any communication among persons related by common ownership or affiliated by corporate control of information in a report containing information solely as to transactions or experiences between the consumer and the person making the report ("transaction/experience" information).

In addition, a consumer report does not include communication of information other than "transaction/experience" information among persons related by common ownership or affiliated by corporate control, if it is clearly and conspicuously disclosed to the consumer that the information may be communicated among such persons and the consumer is given the opportunity, before the time that the information is initially communicated, to direct that such information not be communicated among such persons.

Reasonable Disposal Measures

Q12: What does "disposal" of consumer report information mean?

A12: "Disposal" means either: (1) the discarding or abandonment of consumer report information; or (2) the sale, donation, or transfer of any medium, including computer equipment, on which consumer report information is stored. The sale of consumer report information in connection with a business transaction or the transfer of that information for marketing purposes would *not* be considered "disposal."

Q13: Does the disposal rule *require* that advisers destroy or maintain any information?

A13: No. The disposal rule does not require that an adviser maintain or destroy any record pertaining to a customer nor does it affect any legal requirement to maintain or destroy those records. For example, if the record is required to be maintained under the recordkeeping rule (Advisers Act rule 204-2) for 5 years, the disposal aspect would come into play only after the 5 year period had ended and the adviser wished to dispose of the information.

Q14: The rule requires advisers to adopt "reasonable" measures to dispose properly of consumer report information. What should an adviser consider when drafting its disposal rule policies and procedures?

A14: The rule itself does not provide any standards for what are considered reasonable measures. However, the SEC indicated that when an adviser considers what is "reasonable," it should take into account: (1) what is appropriate for its nature, size, and the complexity of its operations; (2) the sensitivity of the consumer report information; (3) the costs and benefits of available disposal methods; and (4) relevant technological changes.

Q15: What methods of disposal are considered "reasonable" measures?

A15: Reasonable measures to protect consumer report information from unauthorized access or use in connection with its disposal could include:

(1) implementing and monitoring compliance with policies and procedures that require the burning, pulverizing, or shredding of paper records containing consumer report information so the information cannot be read or reconstructed;
(2) implementing and monitoring compliance with policies and procedures that require destruction or erasure of electronic media containing consumer report information so the information cannot be read or reconstructed;
(3) after "due diligence," contracting with another party engaged in the business of record destruction to dispose of material, specifically identified as consumer report information, in a way that would be consistent with the disposal rule;
(4) for an adviser that acts directly as a service provider to an entity subject to the disposal rule and maintains or otherwise possesses consumer report information through providing the services, implementing and monitoring compliance with policies and procedures that protect against unauthorized or unintentional disposal of consumer report information and disposing of in accordance with the first two examples; or
(5) incorporating disposal policies and procedures into safeguard policies and procedures, as long as the disposal rule requirements are met for disposal of consumer report information.

Q16: What type of "due diligence" should an adviser do before hiring a third party vendor to discard the firm's consumer report information?

A16: An adviser's due diligence could include: (1) reviewing an independent audit of the disposal company's operations and/or its compliance with the disposal rule; (2) obtaining information about the disposal company from several references or

other reliable sources; (3) requiring that the disposal company be certified by a recognized trade association or similar third party; or (4) taking other appropriate measures to determine the competency and integrity of the disposal company.

Written Policies and Procedures

Q17: Are written disposal policies and procedures required?
A17: The rule does not explicitly require written policies and procedures for disposal of consumer report information. However, the SEC noted in the release adopting the rule that proper disposal policies and procedures are encompassed within, ***and should be a part of***, an adviser's overall written policies and procedures under the safeguard rule. The SEC indicated that reasonable measures "are very likely to require" the establishment of policies and procedures governing disposal and appropriate employee training.

Q18: May advisers incorporate their disposal rule policies and procedures into their safeguard rule policies and procedures?
A18: Yes. This should include an analysis of how a firm's existing privacy safeguards for the safeguard rule, such as administrative, physical, and electronic records/technical safeguards, would apply to disposal of consumer report information. The firm should take care, however, to apply its disposal policies not only to customer records but also to information and to consumer report information as defined by the rules.

Q19: If an adviser hires a third party service provider to dispose of the firm's consumer report information, must the adviser tell the service provider that the adviser is providing the service provider with consumer report information?
A19: Yes.

Compliance Date

Q20: By when must an adviser comply with the disposal rule?
A20: July 1, 2005.

Q21: What if an adviser already has a contract with a third party service provider to dispose of or destroy records that may include consumer report information?
A21: For contracts existing as of January 11, 2005 (the rule's effective date), the SEC provided a year extension for compliance with the disposal rule. These contracts must be in compliance with the rule by July 1, 2006.