FEDERAL RESERVE

press release

For immediate release January 24, 1972

The Board of Governors of the Federal Reserve System today announced an amendment to its regulations permitting bank holding companies to act--under the 1970 amendments to the Bank Holding Company Act--as investment advisers to investment companies, including mutual funds. The Board said, however, that a holding company engaging in this activity may not, among other things:

1. Sell or distribute securities of any investment company for which it acts as investment adviser.

2. Act as investment adviser to an investment company that has a name similar to the name of the holding company or any of its subsidiary banks.

3. Purchase for its own account securities of any investment company for which it acts as investment adviser; purchase, at its sole discretion, any such securities in a fiduciary capacity; extend credit to any such investment company; or accept the securities of any such investment company as collateral for a loan to purchase securities of the investment company.

In an amendment to its Regulation Y relating to bank holding companies, the Board said it has determined that acting as investment adviser to companies registered under the Investment Company Act of 1940 is an activity "so closely related to banking or managing or controlling banks as to be a proper incident thereto."

Last year, the Board determined that acting as investment or financial adviser--including adviser to a mortgage or real estate investment trust and furnishing economic or financial information--is a permissible activity for bank holding companies, subject to Board approval in individual cases. Effective February 1, this provision of Regulation Y will read as follows (new language underlined):

"Acting as investment or financial adviser, including (i) serving as the advisory company for a mortgage or a real estate investment trust; (ii) serving as investment adviser, as defined in § 2(a)(20) of the Investment Company Act of 1940, to an investment company registered under that Act; and (iii) furnishing economic or financial information."

Acting as a management consultant is not regarded by the Board as part of this activity and whether to propose this as an activity closely related to banking is still under consideration.

The scope of the activity announced today is spelled out in an interpretation that accompanies the amendment. In general, the Board said a bank holding company may exercise all functions customarily permitted an investment adviser except to the extent limited by the Banking Act of 1933 (frequently called the Glass-Steagall Act).

The Board interpreted the Glass Steagall Act as prohibiting a bank holding company from sponsoring, organizing or controlling a mutual fund. The Board does not believe, however, that this restriction applies to closed-end investment companies as long as they are not primarily or frequently engaged in the issuance, sale and distribution of securities.

A copy of the amendment, together with the accompanying interpretation, is attached.

TITLE 12--BANKS AND BANKING

CHAPTER II--FEDERAL RESERVE SYSTEM

SUBCHAPTER A--BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

[Reg. Y]

PART 225--BANK HOLDING COMPANIES

Nonbanking Activities of Bank Holding Companies

By notice of proposed rulemaking published in the Federal Register on August 25, 1971 (36 F.R. 16695), the Board of Governors proposed to add to the list of activities that it has determined to be closely related to banking or managing or controlling banks (§ 225.4(a) of Regulation Y) the following: "serving as investment adviser to an investment company registered under the Investment Company Act of 1940". A hearing on this proposal was held on November 12, 1971, after a notice thereof was published in the Federal Register on October 29, 1971 (36 F.R. 20779).

Following consideration of the comments received and the record of the hearing, the Board has amended § 225.4(a), effective February 1, 1972, to add the new activity, with a minor modification in language from that proposed, to its list of permitted activities.

An accompanying interpretation expresses the Board's views on several questions, which arose during the course of its consideration of this matter, concerning the scope of the new activity and the applicability of certain provisions of the Banking Act of 1933 (48 Stat. 162) thereto.

The text of the amendment to § 225.4(a) reads as follows:

§225.4 Nonbanking activities.

(a) Activities closely related to banking or managing or controlling banks. * * * The following activities have been determined by the Board to be so closely related to banking or managing or controlling banks as to be a proper incident thereto:

* * *

(5) acting as investment or financial adviser, including (i) serving as the advisory company for a mortgage or a real estate investment trust; (ii) serving as investment adviser, as defined in § 2(a)(20) of the Investment Company Act of 1940, to an investment company registered under that Act; and (iii) furnishing economic or financial information;[**]

Effective date: February 1, 1972.

By order of the Board of Governors, January 20, 1972.

(Signed) Tynan Smith

Tynan Smith
Secretary of the Board

(SEAL)

[**] For an interpretation relating to the scope of the activity described in (ii) see 12 CFR 225.125. Acting as a management consultant is not regarded by the Board as within this activity (5). Whether to propose expanding activity (5) to include management consulting is under consideration by the Board.

TITLE 12--BANKS AND BANKING

CHAPTER II--FEDERAL RESERVE SYSTEM

SUBCHAPTER A--BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

[Reg. Y]

PART 225--BANK HOLDING COMPANIES

Nonbanking Activities of Bank Holding Companies

§ 225.125 Investment Adviser Activities.

(a) Effective February 1, 1972, the Board of Governors amended § 225.4(a) of Regulation Y to add "serving as investment adviser, as defined in § 2(a)(20) of the Investment Company Act of 1940, to an investment company registered under that Act" to the list of activities it has determined to be so closely related to banking or managing or controlling banks as to be a proper incident thereto. During the course of the Board's consideration of this amendment several questions arose as to the scope of such activity, particularly in view of certain restrictions imposed by sections 16, 20, 21 and 32 of the Banking Act of 1933 (12 U.S.C. 24, 377, 378, 78) (sometimes referred to hereinafter as the "Glass-Steagall Act provisions") and the United States Supreme Court's decision in Investment Company Institute v. Camp, 401 U.S. 617 (1971). The Board's views with respect to some of these questions are set forth below.

(b) It is clear from the legislative history of the Bank Holding Company Act Amendments of 1970 (84 Stat. 1760) that the Glass-Steagall Act provisions were not intended to be affected thereby. Accordingly, the Board regards the Glass-Steagall Act provisions and the Board's prior interpretations thereof as applicable to a holding company's activities as an investment adviser. Consistently with the spirit and purpose of the Glass-Steagall Act, this

interpretation applies to all bank holding companies registered under the Bank Holding Company Act irrespective of whether they have subsidiaries that are member banks.

(c) Under § 225.4(a)(4), as amended, bank holding companies (which term, as used herein, includes both their bank and nonbank subsidiaries) may, in accordance with the provisions of § 225.4(b), act as investment advisers to various types of investment companies, such as "open-end" investment companies (commonly referred to as "mutual funds") and "closed-end" investment companies. Briefly, a mutual fund is an investment company which, typically, is continuously engaged in the issuance of its shares and stands ready at any time to redeem the securities as to which it is the issuer; a closed-end investment company typically does not issue shares after its initial organization except at infrequent intervals and does not stand ready to redeem its shares.

(d) The Board intends that a bank holding company may exercise all functions that are permitted to be exercised by an "investment adviser" under the Investment Company Act of 1940, except to the extent limited by the Glass-Steagall Act provisions, as described, in part, hereinafter.

(e) The Board recognizes that presently most mutual funds are organized, sponsored and managed by investment advisers with which they are affiliated and that their securities are distributed to the public by such affiliated investment advisers, or subsidiaries or affiliates thereof. However, the Board believes that (i) the Glass-Steagall Act provisions do not permit a bank holding company to perform all such functions, and (ii) it is not necessary for a bank holding company to perform all such functions in order to engage effectively in the described activity.

(f) In the Board's opinion, the Glass-Steagall Act provisions, as interpreted by the U.S. Supreme Court, forbid a bank holding company to sponsor, organize or control a mutual fund. However, the Board does not believe that such restrictions apply to closed-end investment companies as long as such companies are not primarily or frequently engaged in the issuance, sale and distribution of securities. In no case, however, should a bank holding company act as investment adviser to an investment company which has a name that is similar to, or a variation of, the name of the holding company or any of its subsidiary banks.

(g) In view of the potential conflicts of interests that may exist, a bank holding company and its bank and nonbank subsidiaries should not (i) purchase for their own account securities of any investment company for which the bank holding company acts as investment adviser; (ii) purchase in their sole discretion, any such securities in a fiduciary capacity (including as managing agent); (iii) extend credit to any such investment company; or (iv) accept the securities of any such investment company as collateral for a loan which is for the purpose of purchasing securities of the investment company.

(h) A bank holding company should not engage, directly or indirectly, in the sale or distribution of securities of any investment company for which it acts as investment adviser. Prospectuses or sales literature should not be distributed by the holding company, nor should any such literature be made available to the public at any offices of the holding company. In addition, officers and employees of bank subsidiaries should be instructed not to express any opinion with respect to advisability of purchase of securities of any investment company for which the bank holding company acts as investment adviser. Customers of banks in a bank holding company system who request information on an unsolicited basis regarding any investment company for which the bank holding company acts as investment adviser may be

furnished the name and address of the fund and its underwriter or distributing company, but the names of bank customers should not be furnished by the bank holding company to the fund or its distributor. Further, a bank holding company should not act as investment adviser to a mutual fund which has offices in any building which is likely to be identified in the public's mind with the bank holding company.

(i) Acting in such capacities as registrar, transfer agent, or custodian for an investment company is not a selling activity and is permitted under § 225.4(a)(4) of Regulation Y. However, in view of potential conflicts of interests, a bank holding company which acts both as custodian and investment adviser for an investment company should exercise care to maintain at a minimal level demand deposit accounts of the investment company which are placed with a bank affiliate and should not invest cash funds of the investment company in time deposit accounts (including certificates of deposit) of any bank affiliate.

(Interprets and applies 12 U.S.C. 1843(c)(8).)

By order of the Board of Governors, January 20, 1972.

(Signed) Tynan Smith

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Tynan Smith
Secretary of the Board

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