

**MEMO# 1924**

May 17, 1990

## **BANK ASSOCIATION PETITIONS FED FOR MUTUAL FUND POWERS**

May 17, 1990 TO: BOARD OF GOVERNORS NO. 37-90 RE: BANK ASSOCIATION PETITIONS FED FOR MUTUAL FUND POWERS

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As you know, the Federal Reserve Board has issued orders authorizing subsidiaries of bank holding companies to underwrite debt and equity securities, except mutual fund shares. The Institute consistently has taken the position that the Board lacks the legal authority to permit bank holding companies to sponsor and underwrite mutual funds. Under prior Board interpretations, any such mutual funds would be considered affiliates of the bank holding company, which would be principally engaged in distributing their shares to the public and therefore in violation of the Glass-Steagall Act. The Association of Bank Holding Companies has petitioned the Federal Reserve Board to expand the scope of permitted activities for bank holding companies under Regulation Y. One of the additional activities being requested is mutual fund distribution. Specifically, the association requests that the Board amend its regulations to permit bank holding companies to distribute shares of mutual funds advised by affiliates. In support of its request, the association argues that banks have provided similar services (e.g., common trust funds), that banks are already involved in many aspects of the mutual funds business (e.g., brokerage, sweep accounts), that the fund industry is highly concentrated, and that the risks to the banking organization would be minimal. The association also argues that the activities would not violate the Glass-Steagall Act (1) provided the subsidiary would not be "engaged principally" in such activities and (2) if the mutual fund's board were independent in accordance with the "Investment Advisors Act of 1940" [sic]. (The association claims that if the board were independent, the fund would not be "controlled" by the bank holding company and therefore would not be an affiliate.) The petition also requests further amendments to the Board's regulations, including raising the revenue limit for Section 20 subsidiaries to 25% and relaxing certain firewalls. The petition also requests that the provision of any new financial product be considered a permitted "incidental power" during its early development (i.e., research and test marketing). Only when the product is ready for "full production" would the Board be required to consider it on its individual merits. A copy of the petition is attached. We will keep you advised of developments in this area. Craig S. Tyle Associate General Counsel Attachment