

---

**Office of the Comptroller of the Currency  
Federal Deposit Insurance Corporation  
Board of Governors of the Federal Reserve System  
Office of Thrift Supervision**

---

**January 5, 2004**

**Interagency Policy on Banks/Thrifts Providing Financial Support to Funds  
Advised by the Banking Organization or its Affiliates**

**Purpose and Scope**

This interagency policy is issued jointly by the federal banking agencies, including the Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance Corporation (FDIC), the Board of Governors of the Federal Reserve System (Board), and the Office of Thrift Supervision (OTS) (the agencies) to alert banking organizations, including their boards of directors and senior management, of the safety and soundness implications of and the legal impediments to a bank providing financial support to investment funds<sup>1</sup> advised by the bank, its subsidiaries, or affiliates. A banking organization's investment advisory services can pose material risks to the bank's liquidity, earnings, capital, and reputation, and can harm investors, if the associated risks are not effectively controlled. The agencies have concluded that recent market developments, including market volatility, the continued low interest rate environment, and operational and corporate governance weaknesses, warrant the issuance of this guidance.

Banks are under no statutory requirement to provide financial support to the funds they advise; however, circumstances may motivate banks to do so for reasons of reputation risk and liability mitigation. This type of support by banking organizations to funds they advise has included credit extensions, cash infusions, asset purchases, and acquisition of fund shares. In very limited circumstances, certain arrangements between banks and funds they advise have been expressly determined to be legally permissible and safe and sound when properly conducted and managed. However, the agencies are concerned about other occasions when emergency liquidity needs may prompt banks to support their advised funds in ways that raise prudential and legal concerns.

Federal laws and regulations place significant restrictions on transactions between banks and their advised funds. In particular, sections 23A and 23B of the Federal Reserve Act and the Board's Regulation W (12 CFR 223) place quantitative limits and collateral and market terms requirements on many transactions between a bank and certain of its advised funds.

---

<sup>1</sup> Bank advised investment funds include mutual funds, alternative strategy funds, collective investment funds, and other funds where the bank, its subsidiaries, or affiliates is the investment adviser and receives a fee for its investment advice. For purposes of this guidance, "banks" includes banks and savings associations regulated by the federal banking or thrift agencies.

Additionally, the OCC's fiduciary activities regulation (12 CFR 9) may restrict transactions between a bank and its advised funds.<sup>2</sup>

### **Policy**

To avoid engaging in unsafe and unsound banking practices, banks should adopt appropriate policies and procedures governing routine or emergency transactions with bank advised investment funds. Such policies and procedures should be designed to ensure that the bank will not (1) inappropriately place its resources and reputation at risk for the benefit of the funds' investors and creditors; (2) violate the limits and requirements contained in sections 23A and 23B of the Federal Reserve Act and Regulation W, other applicable legal requirements, or any special supervisory condition imposed by the agencies; or (3) create an expectation that the bank will prop up the advised fund. Further, the agencies expect banking organizations to maintain appropriate controls over investment advisory activities<sup>3</sup> that include:

- Establishing alternative sources of emergency support from the parent holding company, non-bank affiliates or external third parties prior to seeking support from the bank.
- Instituting effective policies and procedures for identifying potential circumstances triggering the need for financial support and the process for obtaining such support. In the limited instances that the bank provides financial support, the bank's procedures should include an oversight process that requires formal approval from the bank's board of directors, or an appropriate board designated committee, independent of the investment advisory function. The bank's audit committee also should review the transaction to ensure that appropriate policies and procedures were followed.
- Implementing an effective risk management system for controlling and monitoring risks posed to the bank by the organization's investment advisory activities. Risk controls should include establishing appropriate risk limits, liquidity planning, performance measurement systems, stress testing, compliance reviews, and management reporting to mitigate the need for significant bank support.
- Implementing policies and procedures that ensure that the bank is in compliance with existing disclosure and advertising requirements to clearly differentiate the investments in advised funds from obligations of the bank or insured deposits.
- Ensuring proper regulatory reporting of contingent liabilities arising out of its investment advisory activities in the banking organization's published financial statements in accordance with FAS 5, and fiduciary settlements, surcharges, and other losses arising out of its

---

<sup>2</sup> Banks should be aware that other legal requirements may also restrict or prohibit transactions between a bank and its advised funds, including the Investment Company Act of 1940, the Investment Advisers Act of 1940, and the Employee Retirement Income Security Act of 1974 (ERISA).

<sup>3</sup> The agencies acknowledge the SEC's functional regulatory authority over the investment advisory activities of SEC registered investment advisers. However, the agencies remain responsible for evaluating the consolidated risk profiles of banking organizations, which may include assessing the risks posed to the bank from the activities and obligations of any subsidiary or affiliate.

investment advisory activities in accordance with the instructions for completing Call Report Schedule RC-T – Fiduciary and Related Services.

**Notification**

Because of the potential risks posed by the provision of financial support to advised funds, bank management should notify and consult with its appropriate federal banking agency prior to (or immediately after, in the event of an emergency) the bank providing material financial support to its advised funds. The appropriate federal banking agency will closely scrutinize the circumstances surrounding the transaction and will address situations that raise supervisory concerns.