Meeting Between Staff of the Federal Reserve Board and the Investment Company Institute
February 28, 2018

Participants: Sean Campbell, Anna Harrington, Amy Lorenc, Brian Chernoff, Greg Frischmann, Kirin Walsh (Federal Reserve Board)

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Summary: Staff of the Federal Reserve Board met with representatives of the Investment Company Institute ("ICI") and its members to discuss section 13 of the Bank Holding Company Act of 1956 and its implementing regulations (commonly referred to as the "Volcker Rule"). The representatives of ICI discussed the treatment of U.S. registered investment companies and regulated foreign public funds. These representatives encouraged the Board to consider amending the Volcker Rule's implementing regulations to exclude registered investment companies and regulated foreign public funds from the definition of "banking entity" and to modify the exclusion for foreign public funds from the definition of "covered fund."

Attachment

As of February 28, 2018

Regulated Funds and the Volcker Rule: Three Proposed Revisions

The Volcker Rule was never intended to apply to US registered investment companies ("RICs") and similar funds organized outside the United States ("regulated non-US funds"). Yet, the implementing regulations apply the Rule in a manner that, in various circumstances, impedes the organization, sponsorship and operation of regulated funds. The Agencies should adopt **three key revisions** to resolve these issues.

① *Revise the definition of "banking entity" to exclude all RICs*

A. The implementing regulations currently provide a narrow exception to "banking entity'" treatment for seeded funds.

- Under the implementing regulations, a banking entity may hold 25% or more of a RIC during a one-year seeding period and may apply to the Federal Reserve Board ("FRB") for up to two one-year extensions of the seeding period.
- This construct fails to account for prevailing industry and seeding practices in a variety of contexts.
- Multi-year seeding periods are common and necessary to the successful launch of new RICs.

B. To attempt to address this issue, the Agencies issued an FAQ.

- FAQ 16 is helpful, but it does not provide the certainty needed to plan and launch funds, and it does not address other situations in which fund ownership causes "banking entity" issues (*e.g.*, redemption by large shareholder; fund closure).

C. Excluding all RICs from the definition of "banking entity" would be consistent with congressional intent.

② *Revise the definition of "banking entity" to exclude all regulated non-US funds*

A. Regulated non-US funds face additional difficulties under the implementing regulations.

- Unlike for RICs, the implementing regulations give no assurances that a regulated non-US fund generally will not be considered an affiliate of its banking entity sponsor.
- The implementing regulations also do not address the issue of seeding these funds.

B. These questions are addressed exclusively through FAQs that are helpful but provide incomplete solutions.

- Under FAQ 14, the activities/investments of a "foreign public fund" would not be attributed to its banking entity sponsor under certain conditions.
- FAQ 16 (discussed above) provides equivalent treatment for the seeding of a foreign public fund.

C. Excluding all foreign public funds (as redefined below) is the most straightforward and logical solution to treat RICs and regulated non-US funds with parity.

③ *Simplify the exclusion for "foreign public funds" from the definition of "covered fund"*

A. The exclusion is too narrow and imposes unfair burdens, particularly for US banking entities sponsoring regulated non-US funds.

- <u>Ownership</u>: The fund's ownership interests must be sold "predominantly" through public offering(s) outside the United States. The Agencies exclude RICs without any such condition.
  - Practically, distribution often depends on intermediaries and other third parties. Fund sponsors find it difficult, if not impossible, to identify underlying investors.
- <u>Non-affiliates</u>: If a fund's sponsor is a US banking entity, the fund is excluded only if its ownership interests are sold "predominantly" to non-affiliates. The Agencies have not explained why regulated non-US funds "may present heightened risks of evasion."
  - This policy is inconsistent with the regulation of RICs in the United States.
- <u>Home jurisdiction</u>: A fund must be authorized for sale to retail investors in its "home jurisdiction." The "home jurisdiction" prong is unnecessary to ensure that the fund is more similar to a RIC than to a US covered fund.

B. If a fund is (i) organized or formed under non-US law, (ii) authorized for public sale to retail investors and (iii) regulated as a public investment fund, that fund should qualify as a foreign public fund.

For further detail, *see* Letter to the OCC from Paul Schott Stevens, President & CEO, Investment Company Institute (Sept. 21, 2017), available at http://www.ici.org/pdf/30882a.pdf.