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such shares by the bank holding company.

(Interprets and applies 12 U.S.C. 1843 (a) (1), (2), and (c)(9))

[36 FR 21808, Nov. 16, 1971]

§ 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 section 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 U.S. 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)(5), 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 (1) The Glass-Steagall Act provisions do not permit a bank holding company to perform all such functions, and (2) 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. A bank holding company should not 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, unless the prospectus of the investment company contains the disclosures required in paragraph (h) of this section. In no case should a bank holding company act as investment adviser to an investment company that has either the same

name as the name of the holding company or any of its subsidiary banks, or a name that contains the word ''bank.''

(g) In view of the potential conflicts of interests that may exist, a bank holding company and its bank and nonbank subsidiaries should not purchase in their sole discretion, in a fiduciary capacity (including as managing agent), securities of any investment company for which the bank holding company acts as investment adviser unless, the purchase is specifically authorized by the terms of the instrument creating the fiduciary relationship, by court order, or by the law of the jurisdiction under which the trust is administered.

(h) Under section 20 of the Glass-Steagall Act, a member bank is prohibited from being affiliated with a company that directly, or through a subsidiary, engages principally in the issue, flotation, underwriting, public sale, or distribution of securities. A bank holding company or its nonbank subsidiary may not engage, directly or indirectly, in the underwriting, public sale or distribution of securities of any investment company for which the holding company or any nonbank subsidiary provides investment advice except in compliance with the terms of section 20, and only after obtaining the Board's approval under section 4 of the Bank Holding Company Act and subject to the limitations and disclosures required by the Board in those cases. The Board has determined, however, that the conduct of securities brokerage activities by a bank holding company or its nonbank subsidiaries, when conducted individually or in combination with investment advisory activities, is not deemed to be the underwriting, public sale, or distribution of securities prohibited by the Glass-Steagall Act, and the U.S. Supreme Court has upheld that determination. *See Securities Industry Ass'n* v. *Board of Governors,* 468 U.S. 207 (1984); *see also Securities Industry Ass'n* v. *Board of Governors,* 821 F.2d 810 (D.C. Cir. 1987), *cert. denied,* 484 U.S. 1005 (1988). Accordingly, the Board believes that a bank holding company or any of its nonbank subsidiaries that has been authorized by the Board under the Bank Holding Company Act to conduct securities brokerage activities (either separately or in combination with investment advisory activities) may act as agent, upon the order and for the account of customers of the holding company or its nonbank subsidiary, to purchase or sell shares of an investment company for which the bank holding company or any of its subsidiaries acts as an investment adviser. In addition, a bank holding company or any of its nonbank subsidiaries that has been authorized by the Board under the Bank Holding Company Act to provide investment advice to third parties generally (either separately or in combination with securities brokerage services) may provide investment advice to customers with respect to the purchase or sale of shares of an investment company for which the holding company or any of its subsidiaries acts as an investment adviser. In the event that a bank holding company or any of its nonbank subsidiaries provides brokerage or investment advisory services (either separately or in combination) to customers in the situations described above, at the time the service is provided the bank holding company should instruct its officers and employees to caution customers to read the prospectus of the investment company before investing and must advise customers in writing that the investment company's shares are not insured by the Federal Deposit Insurance Corporation, and are not deposits, obligations of, or endorsed or guaranteed in any way by, any bank, unless that happens to be the case. The holding company or nonbank subsidiary must also disclose in writing to the customer the role of the company or affiliate as adviser to the investment company. These disclosures may be made orally so long as written disclosure is provided to the customer immediately thereafter. To the extent that a bank owned by a bank holding company engages in providing advisory or brokerage services to bank customers in connection with an investment company advised by the bank holding company or a nonbank affiliate, but is not required by the bank's primary regulator to make disclosures comparable to the disclosures required to be made by bank holding companies providing such services, the bank holding company should require

its subsidiary bank to make the disclosures required in this paragraph to be made by a bank holding company that provides such advisory or brokerage services.

(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.

[37 FR 1464, Jan. 29, 1972, as amended by Reg. Y, 57 FR 30391, July 9, 1992; 61 FR 45875, Aug. 30, 1996; Reg. Y, 62 FR 9343, Feb. 28, 1997]

§ 225.126 Activities not closely related to banking.

Pursuant to section 4(c)(8) of the Bank Holding Company Act and § 225.4(a) of Regulation Y, the Board of Governors has determined that the following activities are not so closely related to banking or managing or controlling banks as to be a proper incident thereto:

(a) Insurance premium funding—that is, the combined sale of mutual funds and insurance.

(b) Underwriting life insurance that is not sold in connection with a credit transaction by a bank holding company, or a subsidiary thereof.

(c) Real estate brokerage (see 1972 Fed. Res. Bulletin 428).

(d) Land development (see 1972 Fed. Res. Bulletin 429).

(e) Real estate syndication.

(f) Management consulting (see 1972 Fed. Res. Bulletin 571).

(g) Property management (see 1972 Fed. Res. Bulletin 652).

[Reg. Y, 37 FR 20329, Sept. 29, 1972; 37 FR 21938, Oct. 17, 1972, as amended at 54 FR 37302, Sept. 8, 1989]

§ 225.127 Investment in corporations or projects designed primarily to promote community welfare.

(a) Under § 225.25(b)(6) of Regulation Y, a bank holding company may, in accordance with the provisions of § 225.23, engage in ''making equity and debt investments in corporations or projects designed primarily to promote community welfare, such as the economic rehabilitation and development of low-income areas.'' The Board included that activity among those the Board has determined to be so closely related to banking or managing or controlling banks as be a proper incident thereto, in order to permit bank holding companies to fulfill their civic responsibilities. As indicated hereinafter in this interpretation, the Board intends § 225.25(b)(6) to enable bank holding companies to take an active role in the quest for solutions to the Nation's social problems. Although the interpretation primarily focuses on low- and moderate-income housing, it is not intended to limit projects under § 225.25(b)(6) to that area. Other investments primarily designed to promote community welfare are considered permissible, but have not been defined in order to provide bank holding companies flexibility in approaching community problems. For example, bank holding companies may utilize this flexibility to provide new and creative approaches to the promotion of employment opportunities for low-income persons. Bank holding companies possess a unique combination of financial and managerial resources making them particularly suited for a meaningful and substantial role in remedying our social ills. Section 225.25(b)(6) is intended to provide an opportunity for them to assume such a role.

(b) Under the authority of § 225.25(b)(6), a bank holding company may invest in community development corporations established pursuant to Federal or State law. A bank holding company may also participate in other civic projects, such as a municipal parking facility sponsored by a local civic organization as a means to promote greater public use of the community's facilities.

(c) Within the category of permissible investments under § 225.25(b)(6)