

April 24, 2024

The Honorable Martin J. Gruenberg  
Chairman  
Federal Deposit Insurance Corporation  
550 17<sup>th</sup> Street, NW  
Washington, DC 20429

The Honorable Travis Hill  
Vice Chairman  
Federal Deposit Insurance Corporation  
550 17<sup>th</sup> Street, NW  
Washington, DC 20429

The Honorable Rohit Chopra  
Director  
Consumer Financial Protection Bureau  
1700 G Street, NW  
Washington, DC 20552

Mr. Michael J. Hsu  
Acting Comptroller  
Office of the Comptroller of the Currency  
400 7th Street, SW  
Washington, DC 20219

The Honorable Jonathan McKernan  
Director  
Federal Deposit Insurance Corporation  
550 17<sup>th</sup> Street, NW  
Washington, DC 20429

Re: Regulated Fund Investments in Banking Organizations

Dear Members of the FDIC Board:

On behalf of the Investment Company Institute<sup>1</sup> and its members, I am writing to express concern about recent statements questioning the level of investment in individual banking organizations by regulated

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<sup>1</sup> The [Investment Company Institute](http://www.ici.org) (ICI) is the leading association representing regulated investment funds. ICI's mission is to strengthen the foundation of the asset management industry for the ultimate benefit of the long-term individual investor. ICI's members include mutual funds, exchange-traded funds (ETFs), closed-end funds, and

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funds<sup>2</sup> and yesterday's announcement that the Board of the Federal Deposit Insurance Corporation ("FDIC") will meet tomorrow to discuss proposals related to the Change in Bank Control Act.<sup>3</sup> As you are aware, federal banking agencies have provided regulatory comfort to certain regulated funds in consideration of commitments by those regulated funds and their investment adviser to remain passive investors. In some cases, these letters date back decades. It appears that some Board members may seek to have the FDIC unilaterally revisit this longstanding and well-established approach.

The fact is regulated funds are among the most highly regulated financial products in the United States. They adhere to a uniquely robust regulatory framework that reinforces their fundamental purpose: to invest in securities and other instruments to achieve their stated investment objectives and strategies, providing a means of investment suitable for the general public. Regulated funds play a key role in our economy by channeling significant investment into the US capital markets, fueling economic activity in the United States.<sup>4</sup>

In numerous regulatory determinations to date, the banking agencies have acknowledged the fundamental purpose of regulated funds, as well as the comprehensive regulatory framework applicable to these funds and their advisers, and have concluded that regulated fund investments in securities issued by a banking organization are not made for the purpose of exercising a controlling influence over the management or policies of the banking organization.

Recent statements appear to call into question the current longstanding regulatory approach, relying on vague assertions about investment adviser "influence." To our knowledge, these assertions run counter to the actual commitments made by regulated funds in the course of those regulatory determinations and to regulated funds' actual compliance with those commitments, which compliance has never been questioned in the two decades in which banking agencies have provided comfort to regulated funds. For the same reason, we are skeptical of the need for measures reportedly under consideration, such as establishing a new FDIC monitoring program and constraining regulated fund investments while the FDIC conducts a review.

In the sections below, I explain: (i) the importance of regulated funds to retail investors; (ii) how substantive requirements and regulatory protections distinguish regulated funds from other investors in banking organizations; and (iii) how regulatory determinations to date ensure against an investment adviser and its regulated funds exercising a controlling influence over a banking organization.

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unit investment trusts (UITs) in the United States, and UCITS and similar funds offered to investors in other jurisdictions. Its members manage \$34.4 trillion invested in funds registered under the US Investment Company Act of 1940, serving more than 100 million investors. Members manage an additional \$9.2 trillion in regulated fund assets managed outside the United States. ICI also represents its members in their capacity as investment advisers to certain collective investment trusts (CITs) and retail separately managed accounts (SMAs). ICI has offices in Washington DC, Brussels, and London and carries out its international work through [ICI Global](#).

<sup>2</sup> See, e.g., [Remarks](#) by Jonathan McKernan, Director, FDIC Board of Directors, at the Session on Financial Regulation at the Annual Meeting of the Association of American Law Schools (Jan. 5, 2024); Andrew Ackerman, Regulator Probes BlackRock and Vanguard Over Huge Stakes in U.S. Banks, WSJ (April 2, 2024).

<sup>3</sup> The meeting notice is available [here](#).

<sup>4</sup> See [2023 Investment Company Fact Book](#) at 84-93.

### **Importance of regulated funds to retail investors**

Regulated funds are the original and greatest democratizing force in global financial markets. Today, more than 116 million Americans rely on mutual funds, the most common type of regulated fund, to pursue their financial goals, such as saving for the purchase of a home, preparing for a secure retirement, or paying for higher education.

Fund-owning households represent a broad range of the US population—coming from all age and income groups. The Baby Boom Generation holds the majority of US households’ mutual fund assets, reflecting their immense numbers and the decades they have had to save and invest, but Generation Z and Millennial households also are well on their way to widespread fund ownership. In aggregate, US households’ investment in regulated funds represents about one-fifth of their financial assets, a higher share than seen in other jurisdictions around the world.

To meet the diverse needs of “Main Street” investors, it is no surprise that regulated funds offer a variety of investment objectives and strategies. Some funds are “actively managed” towards a specific objective, while others have an investment objective to follow an index—often referred to as index-based funds.<sup>5</sup> There are a wide variety of indices for index-based investment strategies and a diverse range of active investment strategies.

### **Substantive requirements and regulatory protections distinguish regulated funds from other investors**

Regulated funds are registered under the Investment Company Act of 1940 (“Investment Company Act”) and include mutual funds, ETFs and closed-end funds. The investment adviser to a regulated fund must be registered with the Securities and Exchange Commission (“SEC”) under the Investment Advisers Act of 1940.

Each regulated fund is a separate legal entity, organized under state law usually as a corporation or a business trust (in some states, a “statutory trust”). Regulated funds have officers and directors (if the fund is a corporation) or trustees (if the fund is a trust), including a minimum percentage of independent directors. The regulated fund’s board oversees the management and operations of the fund and has mandated responsibilities under the Investment Company Act. Unlike traditional operating companies, a Regulated Fund is externally managed and typically has no employees in the traditional sense. Instead, a Regulated Fund relies on service providers, including its investment adviser, to invest fund assets and carry out other business activities.

Regulated funds are subject to a comprehensive regulatory scheme under federal securities and other laws. The Investment Company Act and other laws impose substantive requirements on the management and operations of regulated funds as well as extensive disclosure and reporting requirements.

A number of regulated funds may each engage a single investment adviser, but each fund maintains its own agreement with the investment adviser, with its own investment objectives and strategies. The

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<sup>5</sup> At year-end 2022, index mutual funds and index ETFs together accounted for 46 percent of assets in long-term funds. *Id.* at 22, Fig. 2.5.

adviser acts as a fiduciary to each regulated fund and, in this capacity, owes *each fund* a duty of care and a duty of loyalty. The adviser's duty is to manage a regulated fund's assets pursuant to both the separate investment management agreement with that fund and other ancillary documents that set forth the adviser's obligations and other information related to the adviser's management of the fund's assets (e.g., fund prospectus and fund shareholder reports).

Regulated funds and their advisers are also subject to certain proxy voting requirements. In their capacity as shareholders in portfolio companies, regulated funds must disclose their proxy voting policies and procedures and publicly report their proxy votes. Specifically, a regulated fund must (i) describe in its registration statement the policies and procedures that it uses to determine how to vote proxies relating to its portfolio securities<sup>6</sup> and (ii) publicly file with the SEC the fund's records of how it voted proxies relating to its portfolio securities,<sup>7</sup> requirements that the SEC further enhanced in 2022.<sup>8</sup> Regulated funds are unique in this regard—no other type of institutional investor must file with the SEC and publicly disclose how it voted each of its proxies.

Accordingly, SEC regulation of regulated funds and their advisers distinguishes them from other types of investors in banking organizations.

### **Regulatory determinations to date ensure against an investment adviser and its regulated funds exercising a controlling influence over a banking organization**

Regulated funds typically invest in securities (including those issued by banking organizations) for equity exposure and with the expectation of resale, not in order to control companies. This investment-only intent can be discerned from the beneficial ownership filings that regulated funds—both actively managed funds and index funds alike—make with the SEC. Under SEC rules, any person who beneficially owns more than five percent of any class of equity securities must file a publicly available report containing certain information. Regulated funds typically file on Schedule 13G, which is reserved for investors that acquired securities “in the ordinary course of ... business and not with the purpose nor with the effect of changing or influencing the control of the issuer, nor in connection with or as a participant in any transaction having such purpose or effect....” Often the filers of Schedule 13G are referred to as “passive” investors.

In consideration of this status, the Federal Reserve Board (“FRB”) has long provided relief to these passive regulated fund investors, conditional on entering into passivity commitments. These determinations date back to the early 2000's and are memorialized in numerous letters publicly available through the FRB website. Further, the federal banking agencies have also provided relief for years to these passive investors regarding the requirements of Regulation O, conditional on passivity criteria.

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<sup>6</sup> See, e.g., Item 17(f) of Form N-1A.

<sup>7</sup> See Form N-PX (requiring investment companies to file reports with the SEC, not later than August 31 of each year, containing the registrant's proxy voting records for the most recent 12-month period ended June 30).

<sup>8</sup> See [Enhanced Reporting of Proxy Votes by Registered Management Investment Companies; Reporting of Executive Compensation Votes by Institutional Investment Managers](#), SEC Release Nos. 33-11131; 34-96206; IC-34745 (Nov. 2, 2022).

In granting relief, the FRB staff in each instance considered “the nature of [the adviser] and its proposed investments.” The staff recognized that the investments were not proprietary on the part of the adviser but rather were investments *made by* the regulated funds and *on behalf of the beneficial owners of* the regulated funds. The staff acknowledged that the adviser’s regulated funds are not operating companies and that the adviser does not lend to its regulated funds or their portfolio companies. The determinations by the FRB staff recognize that the [adviser] “*is not in the business of operating or controlling*” banking organizations or other companies. In each case, the staff affirmed that “[t]he proposed acquisitions will be made for investment purposes with the expectation of resale and not for the purpose of exercising a controlling influence over the management or portfolio of any [banking organization].”

Regulated funds that have these commitments in place or that rely on the Regulation O relief take very seriously their commitments and periodic certifications they make to the FRB regarding compliance with the commitments. In many cases, these regulated funds may be subject to numerous overlapping passivity requirements under FRB relief, Regulation O relief and SEC requirements relating to the filing of Schedule 13G. Given the extensive commitments to passivity by these funds, a substantial change in regulatory approach is not warranted and risks harming the millions of American families that rely on regulated funds to grow their savings and help them in retirement.

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I look forward to speaking with each of you in more detail about regulated funds and their investments in banking organizations. ICI and its members believe that any unilateral change in policy by the FDIC will be harmful to American investors who rely on regulated funds and the banking organizations that benefit from investments by regulated funds. Please do not hesitate to contact me.

Sincerely,



Eric J. Pan  
President and CEO