Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

Interpretive Letter #1120
August 2009

February 20, 2009

Subject: Request by **[ ]** ("Bank") under Regulation 9 Related to **[ ]**

Dear **[ ]**:

This is in response to your request for OCC confirmation that the Bank may continue to charge fees for admissions and withdrawals from its model-driven funds, where the funds are benchmarked to an index owned and controlled by an affiliated index provider. OCC Interpretive Letter 919 (November 9, 2001) ("OCC IL 919") confirmed that the Bank could charge such fees, provided, in part, that the benchmark index was established and maintained by an independent entity. Based on the Bank's representations and commitments, the Bank may continue to charge fees for admissions and withdrawals from its model-driven funds as described in OCC IL 919, subject to the limitations and conditions set forth below.

Background

The Bank is the trustee for index collective investment funds and model-driven collective investment funds established pursuant to 12 C.F.R. 9.18.[1] A substantial percentage of the Bank's index and model-driven funds are indexed and benchmarked to various fixed income indices formerly owned by **[*ABC*]** (the "**[*ABC*]** Indices"). In September, **[ ]** ("***Affiliate***"), an affiliate of the Bank, acquired the business unit that maintained the **[*ABC*]** Indices.[2]

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[1] Index funds are collective investment funds that seek to replicate the performance of a specified index, such as the Standard and Poor's 500 Index. Model-driven funds are collective investment funds that seek to outperform a specified index or benchmark based on pre-determined investment strategy.

[2] The acquisition closed on Monday, September 22, 2008. **[*Affiliate*]** recently announced that it is rebranding the **[AB*C*]** Indices, along with indices it has established and maintains ("**[*Affiliate*]**Indices"), under the name "**[*Affiliate2*]** Indices." **[*Affiliate*]** is currently maintaining the **[AB*C*]** Indices, with the name of the indices changing from "**[AB*C*]**" to "**[*Affiliate2*]**." **[*Affiliate*]** has stated that it will continue to be able to identify those **[*Affiliate2*]**Indices that are **[AB*C*]**Indices.

The **[*ABC*]** Indices were widely used by institutional asset managers as benchmarks for fixed income index and model-driven collective investment funds. Prior to the acquisition, approximately $4 trillion in assets worldwide were benchmarked to **[*ABC*]** Indices (such as the **[*ABC 3*]** Index), and **[*ABC*]** estimated that more than 90% of fixed income investors in the United States used "**[*ABC*]** Indices as a benchmark. **[*Affiliate*]**, through its acquisition of **[*ABC*]**, has now taken over a significant part of this market. According to the Bank, there is currently no unaffiliated index of a caliber equivalent to certain of the **[*ABC*]** Indices.

OCC Interpretive Letter 919

OCC IL 919 confirmed that it is permissible for the Bank to allocate costs to individual participants being admitted to or withdrawing from model-driven funds in the same manner and to the same extent as section 9.18 index funds. OCC IL 919 also stated that the index the model-driven fund seeks to outperform must be established and maintained by an independent third party. Specifically, footnote 3 stated that:

> [t]he index or benchmark must be established and maintained by an independent organization that is in the business of providing financial information or brokerage services to institutional clients, a publisher of financial news or information or a public stock exchange or association of securities dealers. The index or benchmark must be a standardized index of securities that is not specifically tailored for the use of the manager. [3]

The acquisition of **[*ABC*]**'s index business unit by an affiliate of the Bank raised the issue of whether the Bank was in compliance with that provision of OCC IL 919. On September 19, 2008, the OCC issued a letter to the Bank confirming that, based on the Bank's representations, for the ninety-day period following the acquisition, the Bank could continue to rely on OCC IL 919, and the OCC would deem the Bank's activities not to be inconsistent with OCC IL 919.[4]

The Bank's Request

The Bank now requests that the OCC make the determination it reached in the September 19, 2008 letter permanent with respect to **[*Affiliate*]**'s ownership of the **[*ABC*]** index provider and with respect to any index provider that hereafter may be owned or controlled

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[3] This provision was patterned after the definition of "Index" in the Department of Labor's proposed exemption from prohibited transactions relating to cross-trading under the Employee Retirement Income Security Act of 1974, as amended ("ERISA"). The exemption was proposed in 1999 and adopted by the Department of Labor in 2002 as PTE 2002-12. Department of Labor: Prohibited Transaction Exemption 2002-12, 67 *Federal Register* 6614 (February 12, 2002).

[4] The OCC has granted an extension to the 90 day period. In its request, the Bank had represented that there were sufficient information barriers in place between the Bank and **[*Affiliate*]** to prevent Bank fund managers from controlling or manipulating the **[*ABC*]** Indices. The Bank committed that it would operate in a manner completely separate from the index business. The Bank also noted that the **[*ABC*]** fixed income indices are widely followed benchmarks in the global debt market and had in no way been specifically tailored for the use of the Bank.

by an affiliate of the Bank.[5] The Bank contends that it is not necessary for an index provider to be unaffiliated with or structurally independent of the Bank in order for the OCC to conclude it is permissible for the Bank to allocate costs for admissions and withdrawals.

The Bank argues that the OCC has not imposed this requirement with respect to the allocation of costs to participants in index funds and thus should not impose the requirement on model-driven funds.[6] Moreover, the Bank argues that the rationale for permitting the allocation of costs in model-driven funds, which in the Bank's view is the fair and equitable treatment of participants in the funds, is the same as that for index funds.

The Bank also contends that the critical conditions on which the OCC's interpretation in OCC IL 919 rests were that the allocation of costs must be authorized by the governing documents of the fund, that the index or benchmark must be a standardized index of securities that is not specifically tailored for the use of the fund manager and that the model must be based on prescribed objective criteria using independent third party data that is not within the control of the fund manager.[7] The Bank has represented that it is and will continue to be in compliance with those conditions. The Bank believes these protections are sufficient to ensure that it is properly motivated to act fairly and in the interests of participants in allocating costs to participants admitted to, or withdrawing from, model-driven funds, whether or not the model-driven funds are benchmarked to an index owned and controlled by an affiliate.

To address possible concerns regarding the affiliate relationship, however, the Bank has agreed to comply with additional safeguards to ensure that the subject indices cannot be manipulated or controlled by the Bank.[8] First, the Bank and any affiliated index provider will be separate

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[5] The Bank currently uses only the **[*ABC*]** Indices as benchmarks for its model-driven funds. The Bank has indicated however, that it may want to use one or more of the indices **[*Affiliate*]** established, such as the **[*XX*]** bond Index, **[*XX2*]** Bond Index and **[*XX3*]** Bond Index, as benchmarks for its model-driven funds in the future.

[6] The Bank notes that OCC IL 919 stated that model-driven funds could allocate costs to individual participants being admitted to or withdrawing from such funds *in the same manner and to the same extent as section 9.18 index funds*, provided the fund document authorizes such charges. The Bank cites three OCC interpretations involving index funds noting that none contained a requirement that the index be designed by a person that is unaffiliated with, or independent of, the fund manager. OCC Fiduciary Precedent 9.5980 provides, among other things, that the OCC will not object to the charging of the brokerage fees and expenses to accounts which are purchasing or selling units of an index fund, provided the fund document authorizes such charges. OCC Trust Interpretive Letter No. 228 states that an index fund may charge accounts being admitted to or withdrawn from the fund with trading or market gains or losses, in addition to brokerage expenses. OCC Trust Interpretive Letter No. 232 authorized a bank to make adjustments to unit holdings of certain participants of an index fund to correct an overpayment of transaction costs relating to withdrawals from the fund.

[7] The Bank also represents that it will continue to be subject to all applicable laws, including the fiduciary principles and other provisions of ERISA and fiduciary common law to the extent not preempted by ERISA, which prohibit the Bank from taking any action that is not in the best interests of fund participants or that is inconsistent with the model-driven fund's plan. The OCC has not addressed and does not opine on whether the Bank's use of an index owned and controlled by an affiliate complies with ERISA or applicable federal securities law and state law.

[8] The Bank also has stated that it is in compliance with and will continue to comply with section 23B of the Federal Reserve Act pertaining to its use of the **[*ABC*]** Indices.

business units within the **[*BHC*]**'s group, and the Bank will not exercise direct or indirect control over any affiliated index provider. Second, there will be an effective information barrier between the Bank and any affiliated index provider, such that the Bank would not be provided with access to non-public information regarding the rules, decisions and data underlying the affiliated indices before such information is provided to third parties. Third, the Bank would not have a preferential ability over other similarly situated institutional asset managers to influence the index methodology of an affiliated index. Finally, to the extent the Bank bases its model-driven strategies on products of an affiliated index provider, it will use only indices that are also available for use by unaffiliated institutional asset managers to benchmark index and/or model-driven funds. These safeguards are similar to conditions that the Bank has agreed to with regard to associated requests its affiliates have made to the Department of Labor.

Discussion

OCC IL 919 confirmed that it is permissible for the Bank to allocate costs to individual participants being admitted to or withdrawing from model-driven funds in the same manner and to the same extent as section 9.18 index funds. OCC IL 919 also stated that the index the model-driven fund seeks to outperform must be established and maintained by an independent third party. The purpose of requiring an independent third party was to ensure that the indices used as benchmarks for the Bank's model-driven funds were not within the control of, or subject to manipulation by, the Bank's model-driven fund managers. Based on the commitments set forth above, we believe that this purpose can be achieved by appropriate arrangements even where an affiliate of the Bank owns and maintains the benchmark indices. We further believe that the Bank's commitments and representations provide such appropriate arrangements.

As noted above, the Bank and **[*Affiliate*]** are in separate business units within the **[*BHC*]** group. In addition, the Bank has committed that it will not exercise direct or indirect control over **[*Affiliate*]**. There also are effective business separation policies and procedures in place to restrict the contact and flow of information between the Bank and **[*Affiliate*]**. These policies and procedures will ensure that the Bank will not have access to non-public information regarding the indices before such information is provided to third parties and that the Bank will not receive any benefit from **[*Affiliate*]** from using the **[*ABC*]** Indices that is not available to other unaffiliated asset managers that use the **[*ABC*]** Indices. For these reasons, **[*Affiliate*]** will not be within the control of the Bank and therefore is deemed "independent" of the Bank consistent with OCC IL 919.

Conclusion

Based on the Bank's representations and commitments, the OCC will deem the Bank to be in compliance with the terms of OCC Interpretive Letter 919 with regard to its use of the **[*ABC*]** Indices, subject to the following conditions.

1. The Bank and **[*Affiliate*]** will be separate business units within the **[*BHC*]**'s group, and the Bank will not exercise direct or indirect control over **[*Affiliate*]**.

2. There will be an effective information barrier between the Bank and **[*Affiliate*]**, such that the Bank would not be provided with access to non-public information regarding the rules, decisions and data underlying the affiliated indices before such information is provided to third parties.[9]

3. The Bank will not have a preferential ability over other similarly situated institutional asset managers to influence the index methodology of an affiliated index.

4. To the extent the Bank bases its model-driven strategies on products of an affiliated index provider, it will use only a published index widely used in the market by institutional investors and that is prepared or applied in the same manner for non-affiliated customers as for the Bank.

5. The index will be standardized and will not be specifically tailored for the use of the manager.

6. The model will be based on prescribed objective criteria, using independent third party data that is not within the control of the fund manager.

These conditions are conditions imposed in writing by the agency in connection with the granting of an application or other request within the meaning of 12 U.S.C. § 1818. As such, the conditions are enforceable under 12 U.S.C. § 1818. This determination is limited to the Bank's use of the **[*ABC*]** Indices that were acquired by its affiliate, **[*Affiliate*]**. The Bank must notify the Examiner-in-Charge ("EIC") in writing and must receive written notification of the EIC's supervisory no objection if it decides in the future to use other indices owned and controlled by **[*Affiliate*]** as benchmarks for its model-driven funds. Our conclusions herein are specifically based on the Bank's representations and written submissions. A material change in the facts may result in a different conclusion. If you have any questions concerning this letter, please contact Beth Kirby, Special Counsel, Securities and Corporate Practices Division, at (202) 874-5210.

Sincerely,

signed

Julie L. Williams
First Senior Deputy Comptroller and Chief Counsel

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[9] The Bank may, however, continue to communicate with the **[*Affiliate*]** personnel supporting the **[*ABC*]** Indices in the same manner as the Bank would communicate with unaffiliated index providers, and in the same manner as unaffiliated investment managers may communicate with such **[*Affiliate*]** personnel, including by participating on the same basis as unaffiliated investment managers in any advisory council or similar advisory body through which large institutional investors provide general advice and recommendations regarding the **[*Affiliate2*]** Indices.