



September 25, 2015

**Interpretive Letter #1154**  
**October 2015**  
**12 CFR 9.18(b)(4)(iii)**  
**12 CFR 9.18(c)(5)**

Subject: Request to Operate a Special Exemption Fund Pursuant to Section 9.18(c)(5)

Dear [ ],

This is in response to your letter dated November 19, 2014, in which [ ] (the Bank), requests approval of a special exemption fund pursuant to 12 C.F.R. § 9.18(c)(5). The proposed fund is a short-term investment fund (STIF) with a primary objective of maintaining a stable net asset value (NAV) of one euro (€1.00) per participating interest. For the reasons and subject to the requirements described below, the Office of the Comptroller of the Currency (OCC) grants the Bank's request to operate the special exemption fund described herein.

**Background**

The Bank seeks OCC permission to operate a STIF with a stable NAV of one euro (€1.00) instead of one dollar (the "Euro Fund").<sup>1</sup> Bank clients would use the Euro Fund to invest euros received by them as collateral for securities lending transactions.

The Bank believes that the operation and use of the Euro Fund will permit its customers to earn incrementally greater returns, and may reduce clients' investment risk, compared with investment of cash collateral in a U.S. dollar-denominated STIF. The Bank explains that customers lending euro-denominated securities through the Euro Fund could benefit because borrowers of those securities may be willing to borrow more securities at higher prices when the borrowers are able to post euros as cash collateral. Furthermore, customers are not subject to the risk that their returns will be eroded by currency fluctuations when the securities lent and the collateral for the loan are in the same currency.

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<sup>1</sup> See letter from [ ], to the OCC's [ ], Acting Examiner-in-Charge, Request for Section 9.18(c)(5) Waiver Permitting Euro Denominated Short-Term Investment Fund, November 19, 2014. The Bank has also represented to the OCC that the Euro Fund will not invest in U.S. government or agency obligations.

The Euro Fund is not the first euro-denominated STIF that the Bank has operated. On or about September 20, 2010, the Bank launched a prior STIF denominated in euros (the Prior Euro Fund).<sup>2</sup> The Prior Euro Fund was closed out in December 2011.

The Bank represents that it will operate the Euro Fund in compliance with those provisions of section 9.18(b)(4)(iii) that reference “dollars” or U.S. currency by substituting “euros” or “€” in all dollar-specific references. The Bank also represents that it will operate the Euro Fund in accordance with all other requirements of section 9.18(b)(4)(iii).<sup>3</sup>

## **Discussion**

National banks may invest assets they hold as fiduciary in collective investment funds (CIFs) as provided in 12 C.F.R. § 9.18. CIFs are funds maintained by a bank exclusively for the collective investment and reinvestment of money contributed to the fund by the bank in its capacity as trustee, executor, administrator, guardian, or custodian under a uniform gifts to minors act.<sup>4</sup> A CIF may consist solely of assets of retirement, pension, profit-sharing, stock bonus or other trusts that are exempt from federal income tax.<sup>5</sup> A STIF is a type of CIF that is authorized to value the fund’s assets on a cost basis, rather than a mark-to-market basis, and that follows the requirements of 12 C.F.R. § 9.18(b)(4)(iii). Section 9.18(b)(4)(iii) is designed to address the risk of loss to principal for each participating interest in the STIF and to reduce risks to banks that administer STIFs.<sup>6</sup> Section 9.18(b)(4)(iii) includes a requirement to maintain a NAV of “\$1.00 per participating interest as a primary fund objective.”<sup>7</sup>

Section 9.18 also authorizes the OCC to approve the operation of a “special exemption fund” established by a bank “[i]n any other manner described by the bank in a written plan approved by the OCC.”<sup>8</sup> The written plan must set forth: (i) the reason that the proposed fund requires a special exemption; (ii) the provisions of the proposed fund that are inconsistent with paragraphs (a) and (b) of [12 C.F.R. § 9.18]; (iii) the provisions of paragraph (b) of [12 C.F.R. § 9.18] for which the bank seeks an exemption; and, (iv) the manner in which the proposed fund addresses the rights and interests of participating accounts.<sup>9</sup> Using section 9.18(c)(5) authority, the OCC may permit a bank to operate a STIF that does not comport with a particular provision in section 9.18.

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<sup>2</sup> The regulations in effect at that time did not require the OCC to affirmatively approve the Prior Euro Fund.

<sup>3</sup> The Bank represents that the use of the Euro Fund would be consistent with its status as a fiduciary under the Employee Retirement Income Security Act of 1974, as amended (ERISA) under guidance from the U.S. Department of Labor permitting lending agents, such as the Bank, to accept euro-denominated collateral on behalf of ERISA plans that lend securities.

<sup>4</sup> 12 C.F.R. § 9.18(a)(1).

<sup>5</sup> 12 C.F.R. § 9.18(a)(2).

<sup>6</sup> See 77 Fed. Reg. at 61230-31.

<sup>7</sup> 12 C.F.R. § 9.18(b)(4)(iii)(A).

<sup>8</sup> 12 C.F.R. § 9.18(c)(5).

<sup>9</sup> *Id.* The letter submitted by the Bank meets these requirements.

Section 9.18 contains a number of references to “dollars” or to U.S. currency.<sup>10</sup> These references include a requirement that the STIF operate with a stable NAV of “\$1.00” per participating interest.<sup>11</sup> A STIF is also required to maintain a “dollar-weighted” average portfolio maturity of 60 days or less and a “dollar-weighted” average portfolio maturity of 120 days or less, as determined in the same manner as is required by the U.S. Securities and Exchange Commission (SEC) pursuant to Rule 2a-7 for money market mutual funds (MMFs).<sup>12</sup> Section 9.18 also contains certain other references to U.S. currency, including requirements related to monitoring the fund’s NAV, stress-testing, and disclosures.<sup>13</sup>

### The “\$1.00” NAV Requirement

The Euro Fund could potentially receive and invest euros while maintaining a stable NAV of one dollar (\$1.00) per unit in compliance with the current STIF rules. To do this, however, the fund would have to hedge the risk of foreign exchange fluctuations between the euro and the U.S. dollar. Such an approach would entail greater risks and impose more costs on the STIF than simply denominating the fund in euros. Because the Bank’s proposed STIF will be denominated entirely in one currency (euros), the Euro Fund will not be exposed to greater currency risk than a fund denominated in dollars.<sup>14</sup> Permitting the Euro Fund to operate with a stable NAV of €1.00 will allow the Bank to provide additional services to its customers without subjecting either the Bank or the participating interests in the STIF to any greater risks than those inherent in participating in a dollar-denominated STIF.<sup>15</sup>

### The “Dollar-weighted” Average Requirement

The STIF rules require the maintenance of certain dollar-weighted average portfolio maturities “in the same manner” as required by the SEC pursuant to its MMF rules.<sup>16</sup> This requirement protects STIF participants because securities with shorter periods remaining until maturity generally exhibit a lower level of price volatility in response to interest rate and credit spread fluctuations, and thus provide a greater assurance that the STIF will continue to maintain a stable

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<sup>10</sup> Specifically, there are references to “dollars” or U.S. currency in section 9.18(b)(4)(III) (A), (B), (G)(2), (H)(3), (I), (J)(1), (J)(2), and (K).

<sup>11</sup> 12 C.F.R. § 9.18(b)(4)(iii)(A). The stable NAV requirement was added to the STIF rules in 2012. See 77 Fed. Reg. 61229 (Oct. 9, 2012).

<sup>12</sup> 12 C.F.R. § 9.18(b)(4)(iii)(B).

<sup>13</sup> See 12 C.F.R. § 9.18(b)(4)(iii)(G)(2), (H)(3), (I), (J)(1), (J)(2), and (K).

<sup>14</sup> OCC precedent specifically allows CIFs to invest in international financial markets. See Trust Interpretive Letter #117, 1987 OCC Ltr. LEXIS 94 (September 14, 1987) (OCC would grant approval if requested for national bank to establish CIF providing access to international financial markets).

<sup>15</sup> The euro is one of the most liquid currencies in the world. See Bank for International Settlements, Triennial Central Bank Survey, Foreign Exchange Turnover in April 2013: Preliminary Global Results, at 3, available at <http://www.bis.org/publ/rpfx13fx.pdf> (euro second most traded currency in the world in 2013 after U.S. dollar). Therefore, a fund denominated in euros should have no greater liquidity risk than a fund denominated in dollars and should have no greater difficulty maintaining a stable NAV.

<sup>16</sup> 12 C.F.R. § 9.18(b)(4)(iii)(B).

value.<sup>17</sup> The Bank is able to meet these requirements concerning portfolio weighting for a fund denominated in euros.<sup>18</sup>

### Other References to U.S. Currency in the STIF Rules

12 C.F.R. § 9.18(b)(4)(iii) also contains other references to U.S. currency, which are found in subsections (G)(2), (H)(3), (I), (J)(1), (J)(2), and (K). These other references include requirements related to monitoring the fund's NAV, stress-testing, and disclosures, such as a requirement for the bank to take action when the difference between the mark-to-market net asset value per participating interest and the STIF's amortized cost per participating interest exceeds "\$0.005."<sup>19</sup> These requirements generally relate to how the Bank and the OCC will monitor the performance of the Euro Fund. The Bank can meet the other requirements of 12 C.F.R. § 9.18(b)(4)(iii) for a fund denominated in euros.

### Conclusion

For the reasons described, the Bank's proposed Euro Fund satisfies the purpose of section 9.18(b)(4)(iii) because in the specific case presented the OCC finds that the use of a stable NAV of €1.00, rather than \$1.00, will not materially affect the risk of loss to principal for each participating interest in the STIF and the risks to the Bank. The Bank is a large institution with a demonstrated expertise in operating STIFs. The Bank is requesting a limited exception to the STIF regulations in order to operate the Euro Fund as a STIF in a highly liquid currency. The OCC approves the Bank's request to operate a STIF with a stable NAV of "€1.00" per participating interest as a special exemption fund, provided the Bank complies with all the provisions of 12 C.F.R. § 9.18(b)(4)(iii) that reference "dollars" or U.S. currency as if they instead referenced "euros" or "€" For example, the Euro Fund must maintain a "euro-weighted" average portfolio maturity of 60 days or less and a "euro-weighted" average portfolio maturity of 120 days or less as determined in the same manner as is required by the SEC pursuant to Rule 2a-7 for MMFs, as if Rule 2a-7 required "euro" denomination instead of "dollar" denomination. The Bank must also comply with the other provisions of 12 C.F.R. § 9.18(b)(4)(iii) that reference "dollars" or U.S. currency as if they instead referenced "euros" or "€" specifically subsections (G)(2), (H)(3), (I), (J)(1), (J)(2), and (K).

Our conclusions herein are specifically based on the Bank's representations and written submissions describing the facts and circumstances of the proposed fund. Any change in facts or circumstances or failure to comply with the above requirements could result in a different conclusion, including a determination that the Bank may no longer permissibly operate the Euro

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<sup>17</sup> See 77 Fed. Reg. at 61231 (reasoning behind incorporating these provisions of Rule 2a-7 into STIF rules).

<sup>18</sup> The SEC's MMF Rules contain provisions for determining the maturities of adjustable rate "government securities" when calculating dollar-weighted averages. See 17 CFR 270.2a-7(i)(1). A "government security" is defined as one issued or guaranteed by the United States. See 17 CFR 270.2a-7(a)(17) (citing 15 USC § 80a-2(a)(16)). The Bank has represented that the Euro Fund will not invest in U.S. government or agency obligations.

<sup>19</sup> See 12 C.F.R. § 9.18(b)(4)(iii)(G).

Fund.<sup>20</sup> If you have any questions concerning this letter, please contact David Stankiewicz, Counsel, Securities and Corporate Practices Division, at (202) 649-5510, or Joel Miller, Group Leader for Credit and Market Risk, at (202) 649-6360.

Sincerely,

*Jennifer C. Kelly*

Jennifer C. Kelly  
Senior Deputy Comptroller for Bank Supervision Policy  
and Chief National Bank Examiner

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<sup>20</sup> This approval relates only to one specified fund. Moreover, this approval and the activities and communications by OCC employees in connection with this approval, do not constitute a contract, express or implied, or any other obligation binding upon the OCC, the United States, any agency or entity of the United States, or any officer or employee of the United States, and do not affect the ability of the OCC to exercise its supervisory, regulatory, and examination authorities under applicable law and regulations. The foregoing may not be waived or modified by any employee or agent of the OCC or the United States.