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THE RISE OF MUTUAL FUND ALTERNATIVES: COLLECTIVE INVESTMENT TRUSTS AND RETAIL SEPARATELY MANAGED ACCOUNTS

Participants in the asset management industry have sought out alternatives to mutual funds in recent years, with collective investment trusts and retail separately managed accounts emerging as viable options. The authors address regulatory oversight of these retail alternatives and explore both the benefits and challenges their use may present.

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Even before the U.S. Securities and Exchange Commission proposed comprehensive amendments to various rules under the Investment Company Act of 1940 (the "Investment Company Act") concerning liquidity and dilution management for registered open-end funds, the asset management industry has been adopting alternatives to the mutual fund wrapper. In addition to listed and unlisted closed-end funds and exchange-traded funds, Collective Investment Trusts ("CITs") and retail separately managed accounts ("SMAs") have emerged as attractive alternatives for retail investors and asset managers alike.

This article aims to provide an overview of the CIT and retail SMA landscape. It explores certain regulatory initiatives that may affect these products, and how asset managers can prepare for the increasing investor demand for these products. Finally, it discusses certain compliance and legal obligations associated with managing these products.

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COLLECTIVE INVESTMENT TRUSTS OVERVIEW

The two types of collective funds that are commonly referred to when discussing CITs are: A1 and A2 collective trust funds. On the one hand, an A1 fund, or a Common Trust Fund, is maintained exclusively for the collective investment and reinvestment of money contributed to the collective fund by a bank . . . "in its capacity as trustee, executor, administrator, guardian, or custodian . . . ."[1] On the other hand, A2 CITs consist "solely of assets of retirement, pension, profit-sharing, stock bonus, or other trusts that are exempt from federal income tax."[2] A2 funds have emerged as a popular choice for defined contribution plans, as they are not limited by the bank capacity requirements of A1 funds. The types of plans that can invest in A2 CITs are:

[1] A1 CIT refers to the regulatory standards established under 9.18(a)(1) of the Comptroller of the Currency ("OCC").

[2] A2 CIT refers to the regulatory standards established under 9.18(a)(2) of OCC.

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