OVERTAKING MUTUAL FUNDS: THE HIDDEN RISE AND RISK OF COLLECTIVE INVESTMENT TRUSTS

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Abstract: The retirement security of millions of American workers is increasingly tied to an investment vehicle that most have never even heard of, and whose dramatic rise has received almost no regulatory scrutiny in recent decades. With nearly $7 trillion dollars in assets, "collective investment trusts" (CITs) are rapidly replacing mutual funds on the investment menus of employer-sponsored retirement plans. Individuals who once had staked their retirement nest eggs on the returns from mutual funds have had more and more of their savings transferred into bank-sponsored CITs, which now hold nearly 30% of all assets in defined contribution plans, up from just 13% a decade ago. Legislation to further expand access to CITs is currently pending in Congress. Yet despite such dramatic growth and economic significance, CITs—which look and act a lot like mutual funds but are sponsored by banks and subject to oversight by the Comptroller of the Currency—have been largely overlooked, with almost no critical analysis of CITs as investment funds, as institutional investors, and as increasingly important participants in an interconnected financial system.

This Article tells the story of a century-old bank product seizing on regulatory gaps and exploding in popularity among retirement plans seeking cheaper investment options for individual participants. The dramatic growth of CITs raises new and critical questions about the tradeoffs associated with CITs: in particular, the benefits of lower fees versus the individual and systemic risks that may stem from lower transparency, fragmented regulatory oversight, fewer restrictions on permitted investments, and centralized control in the hands of bank trustees. In identifying these tradeoffs, this Article builds the foundation for future scholarship to improve the understanding of the behemoth investment vehicle whose growth and impact have gone largely unexamined over the last four decades.

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I. INTRODUCTION

The retirement security of millions of American workers is increasingly tied to an investment vehicle that most have never even heard of, and whose dramatic rise has received almost no regulatory scrutiny over the last four decades.[2] With nearly $7 trillion dollars in assets, "collective investment trusts" (CITs)[3] are rapidly replacing mutual funds on the investment menus of employer-sponsored retirement plans in both the private and public sectors.[4] Individuals who once had staked their retirement nest eggs on the returns from mutual funds have had more and more of their savings transferred into bank-sponsored CITs, which now hold nearly 30% of all assets in defined contribution plans, up from just 13% a decade ago.[5] With trillions of dollars in assets and with pending legislation to further expand their reach, CITs are also growing in size and power, not only as retirement savings vehicles, but also as institutional investors acting without the accountability or transparency requirements applicable to mutual funds.[6]

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[2] *See* Elizabeth O'Brien, *These Sneaky Trusts Are Hiding in Your 401(k)*, MONEY (June 21, 2017), http://money.com/money/4807790/low-fee-401k-choices/ [https://perma.cc/SJ4P-TES6] (noting that "[t]here's a stealth investment vehicle that's making its way into more 401(k) plans: the collective investment trust (CIT). You might own one or more, especially if you work for a large company, and not even know it"); Robert S. De Leon, *A Primer on Collective Investment Trusts*, 41 SEC. REGUL. L.J. 5 (2013) (stating that "to most Americans, and many securities lawyers, CITs remain a mystery"); Robert Steyer, *Collective Investment Trusts No Longer Just for Big Dogs*, PENSIONS & INVS., July 18, 2022, https://www.pionline.com/defined-contribution/collective-investment-trusts-no-longer-just-big-defined-contribution-plans [perma] (reporting that "[o]nce the province of the biggest of the big defined contribution plans, collective investment trusts have been showing up in merely large plans, midsize plans and small plans" and noting that "the CIT market share has increased every year"); Jane Hodges, *Cheaper Choice in 401(k)s*, WALL ST. J. (Aug. 2, 2010), https://www.wsj.com/articles/SB10001424052748704198004575310551356374466 [https://perma.cc/W23U-JXPR] ("An increasing number of 401(k) plans offer investment options that look a lot like the typical mutual funds. But they're actually a whole different animal—and investors would be smart to know the difference.").

[3] CITs are also known as "collective investment funds" (CIFs). *See* discussion *infra* Part I.

[4] Gary Gensler, Chair, Sec. & Exch. Comm'n, "Bear in the Woods," Remarks Before the Investment Company Institute (May 25, 2023), https://www.sec.gov/news/speech/gensler-remarks-investment-company-institute-05252023#_ftnref27 [https://perma.cc/C2FZ-HGHD] (noting that "[c]ollective investment funds are estimated to be $7 trillion, $5 trillion at the federal level and $2 trillion at the state bank level").

[5] *See* LIA MITCHELL, MORNINGSTAR CTR. FOR RET. & POL'Y STUD., 2023 RETIREMENT PLAN LANDSCAPE REPORT: AN IN-DEPTH LOOK AT THE TRENDS AND FORCES RESHAPING U.S. RETIREMENT PLANS (2023).

[6] *See, e.g.*, Clara Hudson, *Disney, Apple Investors May Vote on AI Proposals, SEC Says*, BLOOMBERG L. (Jan. 4, 2024, 3:17 PM), https://news.bloomberglaw.com/esg/disney-apple-shareholders-may-vote-on-ai-proposals-sec-says [https://perma.cc/W9KD-NJQF] (describing the shareholder proposals submitted to Apple and Disney by "AFL-CIO Equity Index Funds, a collective investment trust for union members' pension plans"). As set forth by the AFL-CIO Investment Trust Corporation, "[t]he BNY Mellon AFL-CIO Equity Index Funds offer competitively-priced, low-cost equity index fund solutions designed to meet the needs of union pension plan investors…. All of the proxies in each of these funds will be voted in accordance with the AFL-CIO's Proxy Voting Guidelines." The Bank of New York Mellon serves as trustee and discretionary investment manager for the fund. *See* BANK OF

What are CITs? Given the lack of familiarity with the term, CITs are commonly defined by reference to or by comparison with the very thing that they are replacing: the mutual fund. For example, they have been described as "a functional equivalent" of mutual funds,[7] as investments that "look and feel a lot like a mutual fund,"[8] and as "the biggest competitive threat" to mutual funds in the defined contribution market.[9]

But CITs are not mutual funds. Although the two are "functionally similar"—both offer pooled investment vehicles that combine assets from eligible investors into a single fund with a specific investment strategy—mutual funds and CITs are subject to very different governance and oversight regimes.[10] While mutual funds are set up by investment management companies, are widely available to the general public and are regulated by the Securities and Exchange Commission (SEC), CITs are set up by banks or trust companies,[11] available to individuals only through employer-sponsored retirement plans,[12]

N.Y. MELLON, BNY MELLON AFL-CIO INDEX STRATEGIES (2022), https://aflcio-itc.com/wp-content/uploads/2022/09/AFL-CIO-Index-Funds-Handout.pdf [https://perma.cc/EJ8G-CUHV].

[7] William P. Wade, *Bank-Sponsored Collective Investment Funds: Analysis of Applicable Federal Banking and Securities Laws*, 35 BUS. LAW. 361, 364–65 (1980); *see also* ERACH DESAI & JASON DAUWEN, DST SYSTEMS, COLLECTIVE INVESTMENT TRUSTS—A PERFECT STORM 4 (2017), https://www.ctfcoalition.com/portalresource/AM-WP-CollectiveInvestmentTrustsAPerfectStorm-030317.pdf [perma] (suggesting that "CITs are essentially a functional equivalent of mutual funds—basically another comingled investment vehicle").

[8] O'Brien, *supra* note 2 (reporting that "a trust could track the S&P 500 stock index, just like an index mutual fund. There are also target-date trusts: Some plans might offer the Vanguard Target Retirement 2030 Fund, and others, the Vanguard Target Retirement 2030 Trust").

[9] Hannah Glover, *Collective Investment Trusts Muscle in on DC Market*, FIN. TIMES (Sept. 13, 2009), https://www.ft.com/content/f8232374-9eff-11de-8013-00144feabdc0 [https://perma.cc/T5W7-UBHB] (quoting an analyst with Cerulli Associates).

[10] *See* discussion *infra* Part I.

[11] CITs may be established by trust companies or banks under state law, or by national banks under federal law. The Office of the Comptroller of the Currency (OCC) regulations permit a "national bank" to invest assets that it holds as fiduciary in "collective investment funds." 12 C.F.R. § 9.18(a) (2022). The OCC explains that "[a] collective investment fund (CIF) is a bank-administered trust that holds commingled assets that meet specific criteria established by 12 CFR 9.18. The bank acts as a fiduciary for the CIF and holds legal title to the fund's assets. CIFs allow banks to avoid costly purchases of small lot investments for their smaller fiduciary accounts." *Collective Investment Funds*, U.S. OFF. OF THE COMPTROLLER OF THE CURRENCY, https://www.occ.treas.gov/topics/supervision-and-examination/capital-markets/asset-management/collective-investment-funds/index-collective-investment-funds.html [https://perma.cc/9Y3T-SWTK].

[12] Whereas mutual funds are marketed and available to retail or individual participants, CITs are only available to individuals through employer-sponsored retirement plans. Only certain types of retirement plans (such as 401(k) plans, 457(b) plans, qualified profit-sharing plans, qualified pension plans, and Taft Hartley plans) are currently allowed to participate in CITs. The OCC restricts advertising to the general public. ("A bank may not advertise or publicize any fund authorized under paragraph (a)(1) of this section, except in connection with the advertisement of the general fiduciary services of the bank.") 12 C.F.R. § 9.18(b)(7) (2022).

and regulated primarily by the Office of the Comptroller of the Currency (OCC) and, in some cases, by the Department of Labor (DOL).[13]

Relative to mutual funds, CITs face fewer restrictions on the types and composition of permissible investments,[14] and fewer registration and reporting requirements. CITs and CIT interests are exempt from registration with the SEC under the Investment Company Act of 1940 and the Securities Act of 1933. As a result, CITs are not subject to the substantive requirements under those laws.[15] For example, since they are normally exempt from SEC registration, CITs do not need a registration statement or a prospectus for prospective purchasers. Since there is no registration, there are no registration fees to be paid to the SEC, and no registration statement subject to SEC review. Similarly, although CITs, like mutual funds, hold shares of public companies and exercise the corporate voting rights afforded to such shares, CITs are not subject to the securities law requirements to disclose their voting records publicly,[16] or to give fund investors

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[13] When CITs are established by a bank or trust company that is federally chartered, the CITs are regulated by the OCC. CITs sponsored by state-chartered banks or trust companies are regulated by state authorities. The Department of Labor also has oversight authority over most CITs through its oversight of the retirement plans that invest in CITs. If a plan that is subject to the Employee Retirement Income Security Act of 1974 (ERISA) includes a CIT as an investment option on its menu, the CIT trustee is generally required to comply with ERISA's fiduciary standards in managing the CIT. The trustee of a mutual fund would not be required to comply with these ERISA standards. *See* Noah Zuss, *CITs Have Different Fiduciary Implications than Mutual Funds*, PLANADVISER (Mar. 30, 2022), https://www.planadviser.com/cits-different-fiduciary-implications-mutual-funds/ [https://perma.cc/E8F5-GUXU] ("CITs are plan asset vehicles for ERISA purposes, which means that ERISA standards of prudence and loyalty apply to those who manage and exercise discretionary authority over a plan's assets . . . . Therefore, trustee banks responsible for managing CIT assets are subject to ERISA's fiduciary standard.").

[14] For example, unlike mutual funds, CITs may invest in futures and commodities, commercial real estate, and private equity interests without regulatory restrictions on the amount of such investments. De Leon, *supra* note 2, at 1. CIT providers emphasize the availability of "innovative investment strategies." *See, e.g.,* State Street, Collective Investment Trust Solutions, https://www.statestreet.com/us/en/asset-owner/solutions/collective-investment-trust-solutions (noting that "CITs can offer strategies with broader flexibility of investment options than 1940 Act structures" including but are not limited to, "derivatives, bank debt, ETFs, private equity and real estate," and emphasizing that "CITs are not constrained by an illiquidity cap found in other investment vehicles"); Alex Ortolani, *Fidelity Launches CITs With Alternative Investment Exposure*, PLANADVISER (Nov. 1, 2023), https://www.planadviser.com/fidelity-launches-cits-alternative-investment-exposure/ [https://perma.cc/L4JL-VRTM] (noting that the "[n]ation's largest recordkeeper seeks to bring direct real estate investing to plan participants").

[15] *Why Collective Investment Trusts Are Gaining Traction Within DC Retirement Plans,* WELLINGTON MGMT. CO. (Aug. 2022), https://www.wellington.com/en/insights/collective-investment-trusts-dc-retirement-plans [https://perma.cc/7KHP-V4UA]; *see also infra* Part I.

[16] *See, e.g.*, Jeff Sommer, *Want a Bigger Say on Corporate Behavior? Move Your Money*, N.Y. TIMES (Dec. 12, 2019), https://www.nytimes.com/2019/12/12/business/corporate-behavior-move-your-money.html [https://perma.cc/3MUC-9PWM] (arguing that "[m]illions of people have a stake in corporate America through mutual funds" and reporting on Morningstar's analysis of "every proxy vote cast by the big mutual fund companies in 2019"). The analysis described in the article is possible because registered investment funds (i.e. mutual funds) are subject to disclosure requirements under the Investment Company Act of 1940.

"voice" in fund governance. Instead, CITs entrust exclusive management responsibility with the bank trustees who cast votes on behalf of the trusts.[17] As a result, "it is faster and cheaper to create and launch a CIT than a comparable mutual fund."[18] And even after formation, there is widespread consensus that CITs are subject to fewer regulatory requirements and constraints.[19]

The lower compliance and marketing costs are credited as a key reason for CITs having lower fees than comparable mutual funds.[20] Morningstar, whose subsidiary provides advisory services to CITs, reports that "when comparing the net expense ratio of CIT tiers and mutual fund share classes of the same strategy, CITs are cheaper 88% of the time; and considering only the least-expensive CIT tier and mutual fund share class, CITs are cheaper 92% of the time."[21] According to Morningstar calculations, "[a]cross all investment strategies, as of year-end 2020, the average passive CIT costs less than the average passive mutual fund. Similarly, the average active CIT costs 60% less than the average active mutual fund."[22]

The cost differences matter because even seemingly small differences are compounded over decades.[23] In an environment where retirement plan sponsors (i.e., the employers) have faced significant litigation risk over excessive retirement plan fees,[24] the existence of lower fee options that offer the same or similar investment strategies to those offered by mutual funds has precipitated the exodus out of mutual funds in favor of CITs. Importantly, the management

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17 *See infra* Section II.B.

18 De Leon, *supra* note 2, at 2.

19 *See, e.g.*, Thomas Roberts & James E. Bowlus, *Collective Investment Trusts and Good Governance Considerations*, WILMINGTON TRUST 1 (2022), https://www.wilmingtontrust.com/content/dam/wtb-web/pdfs/cit-whitepaper-2022.pdf [https://perma.cc/U3FK-U5D5] (emphasizing that "the exemptions from registration under the federal securities laws available to CITs may afford them cost advantages relative to their mutual fund counterparts, because CITs can avoid the expenses associated with mutual fund registration, prospectus, and annual report updating and mailing, and the like").

20 *See, e.g.*, MITCHELL, *supra* note 5, at 25 ("This difference in costs is mostly because CITs are not marketed nor regulated in the way that mutual funds are."). Numerous industry publications provide statistics on the cost-savings associated with CITs. *See*, *e.g.*, *What's New? Even Lower Costs and a New Retirement Income Option*, VANGUARD (Sept. 28, 2021), https://institutional.vanguard.com/insights-and-research/perspective/whats-new-even-lower-costs-and-a-new-retirement-income-option.html [https://perma.cc/NMY2-HUFS]; WELLINGTON MGMT. CO., *supra* note 15 (suggesting "that fees for CITs may be between 10 and 30 basis points (bps) lower than for mutual funds of similar composition").

21 MITCHELL, *supra* note 5, at 25 Morningstar also reports that "[t]he asset-weighted average expense ratios of both active and passive CITs are less than half those of their mutual fund counterparts." *Id.*

22 *Id.* at 25.

23 As the Department of Labor has warned, over thirty-five years, a "1 percent difference in fees and expenses [reduces an] account balance at retirement by 28 percent. *A Look at 401(k) Plan Fees*, U.S. DEP'T OF LAB. 2 (Sept. 2019), https://www.dol.gov/sites/dolgov/files/ebsa/about-ebsa/our-activities/resource-center/publications/a-look-at-401k-plan-fees.pdf [https://perma.cc/LB6B-XD86].

24 Natalya Shnitser, *The 401(k) Conundrum in Corporate Law*, 13 HARV. BUS. L. REV. 289 (2023) (describing the nearly 800 fee litigation cases brought against plan sponsors over the last fifteen years).

companies most commonly associated with mutual funds—including Fidelity, Vanguard, and State Street—have all started to offer CITs through affiliated trust companies or banks.[25]

The growth of CITs over the last decade has outpaced all predictions,[26] with CITs now "a standard part of the largest plans in the U.S.," and increasingly present in plans of all sizes[27] in both the public and private sectors.[28] Plans menus that once included primarily mutual funds now increasingly offer CITs. Target date funds, which have been particularly popular on retirement plan investment menus, are now offered through CIT vehicles rather than mutual funds.[29] The same is true for equity, debt, and alternative investment strategies. Consider, for example, the Facebook/Meta Platforms Inc. 401(k) Plan. In 2009, nearly all the assets in the plan were invested in mutual funds. By 2021, nearly all the assets in the plan were invested in collective investment trusts.[30]

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[25] *See* Tim McLaughlin, *U.S. Mutual Funds Cut Expenses by Shifting Billions to Trusts*, REUTERS (Mar. 4, 2015), https://www.reuters.com/article/idUSL1N0W51V8/ [https://perma.cc/H532-UJD2] (reporting that "[m]utual fund companies, including No. 2 Fidelity Investments, have slashed fees on their most popular funds by shifting billions of dollars into collective trusts not regulated by the U.S. Securities and Exchange Commission").

[26] *See, e.g.*, DeLeon, *supra* note 2, at 1 (writing in 2013 that "[a]ssets in collective investment trusts ("CITs") are projected to reach $1.4 trillion, or roughly 20% of the defined contribution market, in 2020"); McLaughlin, *supra* note 25 (noting that "[i[n recent years, research firms have estimated that CIT assets would top $2 trillion in 2015. But a Reuters analysis of disclosures by trust banks, including ones operated by BlackRock Inc, State Street Inc and Wellington Management, reveal that figure was easily surpassed in 2014").

[27] MITCHELL, *supra* note 5, at 4 (noting that "the largest plans in the U.S . . . . [t]oday hold nearly 88% of all the collective investment trust, or CIT, assets" and emphasizing that "CITs have doubled their share of the pie among the largest plans from 17% of assets in 2012 to 36% in 2021"). Morningstar also notes that "[u]sage among plans with fewer than $500 million in assets grew by more than 10% in 2020 and 2021, suggesting CITs may finally break the smaller plan barrier soon." *Id.* at 23.

[28] For examples of CITs in both public and private plans, including the federal government Thrift Savings Plan, *see, e.g.,* Employee Benefits Security Administration, Performance Audit of Thrift Savings Plan Investment Management Operations, Sept. 4, 2020, https://www.dol.gov/sites/dolgov/files/EBSA/about-ebsa/our-activities/resource-center/reports/thrift-savings-plan-audit/investment-management-operations-2020.pdf [perma] (referencing BlackRock's TSF Fund Series and Collective Trust Funds); CalPERs 457 Plan, Fund Fact Sheets, Sept. 2023, http://calpers-sip.com/PDF_InvestmentOps/CalPERS_FFS.pdf [perma](describing the investment options as collective investment trusts); AFL-CIO, Press Release, *AFL-CIO Teams Up with Wilmington Trust and BNY Mellon to Expand Retirement Planning Options for Millions of Americans*, Mar. 22, 2021, https://aflcio.org/press/releases/afl-cio-teams-wilmington-trust-and-bny-mellon-expand-retirement-planning-options [perma] (announcing "a groundbreaking collaboration…to distribute 12 new target date collective investment trust (CIT) funds expanding retirement planning options for its 56 unions and 12.5 million members" and noting that "voting proxies for each fund conform with the AFL-CIO's Proxy Voting Guidelines, per an independent proxy voting fiduciary").

[29] CITs made up 47% of target-date strategy assets as of the end of 2022 and are projected to become the most popular target-date vehicle by 2024. *See* Morningstar, Target-Date Strategy Landscape: 2023 (2023).

[30] Facebook/Meta 401(k) Plan Form 5500s offer the relevant comparison: As of 2009, all plan assets were held in mutual funds (and one money market fund). By 2021, nearly all the assets were held in one of seventeen collective investment trust (and one mutual fund and one money market fund).

According to Morningstar, "[t]he largest plans in the U.S. started to abandon mutual funds 10 years ago" and since 2012, CITs have grown from 13% of assets in DC plans, up to 28% of assets in 2021.[31] The growth of assets in CITs has dramatically outpaced the growth of assets in retirement plans generally, and the growth of assets in mutual funds.[32] Even smaller employers have begun to add CIT options on plan menus,[33] while CIT sponsors and industry advocates have been lobbying Congress to make CITs available to retirement plans in the non-profit and higher-education sectors, which have not been allowed to participate in CITs to date.[34] Legislation to expand access to CITs is currently pending in Congress.[35]

The dramatic rise of CITs has not been accompanied by a corresponding increase in scholarly or regulatory analysis. Indeed, although CITs were the subject of robust Congressional and scholarly examination in their early years and through the 1970s, they have received scant scholarly or regulatory attention over the last four decades.[36] This Article begins to fill the gap and makes the

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[31] Morningstar, *supra* note 28, at 24.

[32] WELLINGTON MGMT. CO., *supra* note 15, at fig.1 (reporting that "[f]rom 2015 to 2020, total 401(k) plan assets grew by roughly 62%, while 401(k) assets held in CITs saw growth of 138%"); MITCHELL, *supra* note 5. Morningstar reports that "[s]ince 2012, DC plan CIT assets more than quadrupled from $463 billion to $2.25 trillion, while DC plan mutual fund assets merely doubled from $1.52 trillion to $3.25 trillion." MITCHELL, *supra* note 5, at 24.

[33] MITCHELL, *supra* note 5, at 30 (noting that "[u]sage among plans with fewer than $500 million in assets grew by more than 10% in 2020 and 2021, suggesting CITs may finally break the smaller plan barrier soon"). A recent Fidelity survey revealed that the "the percentage of sponsors beginning to offer CITs had a 10% annual growth rate from 2018 to 2023" with 29% of sponsors surveyed "considering offering CITs for the first time" and 28% of sponsors surveyed considering "increasing the number of CITs." *See* Brian Anderson, *4 Key Findings from Fidelity's Plan Sponsor Attitudes Survey*, 401KSPECIALIST (Aug. 28, 2023), https://401kspecialistmag.com/4-key-findings-from-fidelitys-plan-sponsor-attitudes-survey/ [https://perma.cc/T4VP-3NK8].

[34] For example, in recent Senate hearings "to Examine Investigating Challenges to American Retirement Security," the President of Retirement Plans for Nationwide stated that "we are excited about the opportunity to make collective investment trusts available to 403(b) plans to help more American workers save, especially those in education, health care, and charitable organizations." *Hearings to Examine Investigating Challenges to American Retirement Security: Hearing Before the Subcomm. on Soc. Sec., Pensions, & Fam. Pol'y of the S. Comm. on Fin.*, 116th Cong. 10 (2020) (statement of Eric Stevenson, President, Retirement Plans, Nationwide); *see also* JASMIN SETHI, MORNINGSTAR INC., LIA MITCHELL & ARON SZAPIRO, CTR. FOR RET. & POL'Y STUD., CITS: A WELCOME ADDITION TO 403(B) PLANS (2020).

[35] Brian Croce, *House Committee Advances Bill Allowing 403(b) Plans to Offer CITs*, PENSIONS & INVS., May 25, 2023, https://www.pionline.com/defined-contribution/house-committee-advances-bill-allowing-403b-plans-offer-cits [perma] (noting that Retirement Fairness for Charities and Educational Institutions Act of 2023 would amend federal securities law to authorize the use of CITs within 403(b) plans, and reporting Vanguard's support for the bill).

[36] A literature review reveals a robust regulatory debate, and academic coverage thereof, though the 1970s, but very limited academic coverage of CITs in the years since then. For academic and regulatory analysis of CITs prior to 1980, see Wade, *supra* note 7, at 364–65 (1980); Note, *The Legality of Bank-Sponsored Investment Services*, 84 YALE L.J. 1477 (1975); Louis J. Marin, *Common Trust Funds - Development and Federal Regulation*, 83 BANKING L.J. 565 (1966); John Michael Webb,

case that CITs—although not squarely within the domain of any one academic discipline—should be of interest to scholars of banking law, corporate law, securities law, and employee benefits law. Indeed, their interdisciplinary nature makes CITs an important case study in financial instruments operating at regulatory crossroads and taking advantage of the challenges of inter-agency coordination.

Section II traces the evolution of CITs in the United States, with a particular focus on the dramatic growth of CITs in defined contribution retirement plans. It shows how over the last hundred years, a type of bank trust originally intended for the fiduciary administration of small accounts has evolved and exploded into a powerful industry managing $7 trillion of retirement savings of American workers. The recent exodus of assets from mutual funds into CITs can be explained by three key drivers. First, employer interest in cheaper investment options for plan menus, driven in part by increased retirement fee litigation, has bolstered demand for CITs.[37] At the same time, the competition for the business of managing retirement assets has encouraged not only banks but also mutual fund management companies to ramp up their CIT offerings. The management companies that once lobbied intensely against CITs have set up trust subsidiaries and affiliated banks to establish their own CITs. Once in the CIT business, the financial institutions have likely come to appreciate certain regulatory differences, such as the ability to cast contentious or politically fraught proxy votes without having to report their voting records to the public.[38] In fact, CIT providers are now lobbying Congress to expand access to CIT products.

Comment, *Of Banks and Mutual Funds: The Collective Investment Trust*, 20 SW. L.J. 334 (1966); Note, *Commingled Trust Funds and Variable Annuities: Uniform Federal Regulation of Investment Funds Operated by Banks and Insurance Companies*, 82 HARV. L. REV. 435 (1968); James J. Saxon & Dean E. Miller, *Common Trust Funds*, 53 GEO. L.J. 994 (1965). Since 1980, there have been only a few academic pieces that address or even mention CITs. *See, e.g.*, Howell E. Jackson, *A System of Fiduciary Protections for Mutual Funds*, *in* FIDUCIARY OBLIGATIONS IN BUSINESS (Arthur Laby & Jacob H. Russell eds., 2021) (identifying CITs as an example of “contexts in which mutual fund shares are distributed to retail investors through pooled vehicles not directly subject to mutual fund regulation); David H. Webber, *Reforming Pensions While Retaining Shareholder Voice*, 99 B.U. L. REV. 1001 (2019) (considering the potential of CITs to preserve “shareholder voice”); Edwin J. Elton, Martin J. Gruber & Christopher R. Blake, *The Performance of Separate Accounts and Collective Investment Trusts*, 18 REV. OF FIN., 1717 (2014).

[37] *See, e.g.*, O’Brien, *supra* note 2 (reporting the growing popularity of CITs and noting that “[r]ecent lawsuits filed by retirement-plan participants accusing companies of having excessive 401(k) fees have put a spotlight on what savers pay”).

[38] *See, e.g.*, Justin Worland, *Larry Fink Takes on ESG Backlash*, TIME (June 29, 2023), https://time.com/6291317/larry-fink-esg-climate-action/ [https://perma.cc/XS2N-WY2G] (reporting that as the backlash to ESG has grown over the last year, business leaders have changed the way they talk about their climate work to tiptoe around the political faultlines”); Tony Owusu, *BlackRock, Vanguard ESG Policies Get Political Pushback*, THESTREET (Dec. 12, 2022), https://www.thestreet.com/investors/blackrock-vanguard-esg-policies-get-political-pushback [https://perma.cc/88N6-BN7W].

After describing the growth of CITs, Section II then reviews the unique regulatory framework for CITs and shows that what has made CITs attractive to industry participants may also explain the lack of regulatory and academic attention on these investment vehicles. Next, Section II revives the debate about "functional regulation" and the question of whether similar financial instruments should be regulated similarly. This debate, which featured CITs quite prominently in the 1960s and 1970s, has waned in the ensuing decades. The recent dramatic growth of CITs merits a reopening of the discussion.

Sections III and IV turn to an evaluation of the impact of CITs which, in the absence of "functional regulation," are subject to a regulatory regime that is strikingly different from the one applicable to mutual funds. Section III situates CITs in the theoretical framework for investment funds and shows the outsized role of employers in protecting the interests of individual investors in CITs. It examines CITs' growing shareholder activism, brings to light the lack of proxy vote disclosure requirements, and explores the risks of "financial fires" stemming from regulatory gaps in an interconnected financial system.[39]

Section IV turns to the benefits and costs of CITs as a retirement savings vehicle. It emphasizes that the regulatory framework for CITs predates the rise of defined-contribution retirement plans in which individual participants bear the investment and longevity risks. Although lower fees in retirement plans are an important and attractive feature, the lower fees currently come at the expense of transparency and disclosure, including public disclosure about CIT fees. In the absence of robust public disclosure and public familiarity with CITs, there is increased pressure on plan sponsors (i.e., employers) as ERISA fiduciaries to negotiate and monitor custom fee arrangements with bank trustees. At the same time, the relatively limited public disclosure reduces monitoring by third parties and makes it more difficult for plaintiffs to bring litigation challenging the inclusion of CITs on retirement plan menus. Section V concludes with a call for closer examination of the tradeoffs in the recent embrace and potential expansion of CITs.

II. A Primer on Collective Investment Trusts

Collective investment trusts have been around for nearly a century, although the 2023 and 1923 versions look quite different. This Section first traces the origins and evolution of CITs and then describes how CITs are structured, governed, and regulated today.

[39] Gensler, *supra* note 4 (making the case for additional liquidity and swing pricing rules for mutual funds and lamenting that "[r]ules for [CITs] lack limits on illiquid investments and minimum levels of liquid assets" and that "[t]here is no limit on leverage, requirement for regular reporting on holdings to investors, or requirement for an independent board").

A. The Origins and Evolution of Collective Investment Trusts

The century-old story of CITs reflects the long-standing battle between banks and other financial institutions to manage Americans' savings. The story proceeds in four parts: the rise of collective bank trusts for narrow purposes in the 1920s; the expansion of bank trusts for retirement plan assets in the 1950s; the growth of defined contribution plans and the decline of traditional defined benefit pension plans starting in the 1980s; and, since 2000, a variety of CIT adaptations to better compete with mutual funds.

1. The First Collective Bank Trusts, the 1929 Crash, and the Defining Decades for Banking and Securities Regulation: 1920–1940

The story of collective investment trusts begins in the 1920s when regulators permitted banks to serve as fiduciaries, which allowed the banks to retain and manage the balances of customers following their death and to engage in certain business that was of a "trust nature."[40] Because such accounts were relatively small at the time, regulators allowed banks to commingle and invest "small accounts" held in a fiduciary capacity.[41] The Board of Governors of the Federal Reserve (the Board) maintained that such trusts could be maintained only to facilitate fiduciary account administration, and not as vehicles for investment by the general public. [42]

Such limitations on bank-sponsored trusts reflected the "general public dismay over the role played by banks in the stock market debacle of the late 1920s and early 1930s."[43] In the decades preceding the crash of 1929, banks and trust companies had emerged as competitors in the financial services industry. To compete with trust companies, which could "underwrite or deal in equity

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[40] Carl Zollman, *Fiduciary Power of National Banks Under the Federal Reserve System*, 11 MARQ. L. REV. 39, 39 (1926). The Federal Reserve Act of 1913 had authorized the Federal Reserve Board "to grant by special permit, to national banks applying therefor, when not in contravention of state or local law, the right to act as trustee, executor, administrator, or registrar of stocks and bonds under such rules and regulations as the said board may prescribe." Federal Reserve Act, Pub. L. No. 43-6, § 11 (k), 38 Stat. 251 (1913).

[41] In the 1920s, after "various states enacted legislation authorizing the establishment of common trust funds," the Board of Governors of the Federal Reserve (the Board) enacted a series of exceptions to the prior prohibition on the commingling of trust funds. Wade, *supra* note 7, at 363–64. Favorable tax treatment bolstered the popularity of the common trust fund for small accounts. The Revenue Act of 1936 granted tax-exempt status to common trust funds maintained by a bank, a decision that was based in part on Congressional recognition that common trust funds "serve a good social purpose" by providing investment safety and diversification for accounts "that are small in amount." *Id.* at 364 (citing S. REP. NO. 74-2156, at 20 (1936)).

[42] Board of Governors of the Federal Reserve System, 2 Fed. Reg. 2976 (Dec. 21, 1937). The Federal Reserve Board's regulations mandated that common trust funds be operated in furtherance of "bona fide fiduciary purpose" and not solely as vehicles for investment purposes.

[43] Wade, *supra* note 7, at 365 (citing *Glass-Steagall Act–A History of Its Legislative Origins and Regulatory Construction*, 92 BANKING L.J. 38, 47 (1975)).

as well as debt securities and participate in potentially huge profits (or losses) from speculation," the national banks, which did not have the power to deal in equity securities directly, began to organize "security affiliates" under state law to accomplish their objectives indirectly.[44] Moreover, by establishing what were then called "investment trusts," the security affiliates provided a way for bank shareholders to participate individually in speculative investment activities.[45] Despite warnings of potential abuses within the system, security affiliates were allowed to flourish throughout the 1920s.[46] In the aftermath of the 1929 crash, Congressional investigations revealed that the security affiliate system was beset by numerous abuses stemming from the interdependent financial relationship between many banks and their security affiliates.[47]

The Congressional response came, in part, in the form of the Glass-Steagall Act of 1933,[48] which sought to "prevent recurrence of specific abuses arising from bank involvement in certain securities activities which had apparently aggravated the stock market collapse of 1929."[49] Through the Act, Congress aimed to achieve the "complete divorcement of commercial banking from investment banking."[50] Notably, however, the Act did not prohibit the exercise of fiduciary powers granted banks earlier under the Federal Reserve Act.[51]

The Great Depression also prompted broader financial regulation and securities laws reforms to ensure the stability of the U.S. financial system and capital markets. In addition to the Glass-Steagall Act of 1933, the key reforms included the Securities Act of 1933[52] and the Investment Company Act of 1940.[53] Like the Glass-Steagall Act, the securities laws also included carve-outs for collective trusts.

The Securities Act aimed to curb abuse in a largely unregulated securities market. The Act sought investor protection through disclosure and the

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[44] The typical security affiliate was owned and operated by and for the sponsoring bank and engaged in various underwriting and investment functions on the bank's behalf.

[45] Wade, *supra* note 7, at 373.

[46] *Id.*

[47] *Id.* at 374 ("When either the bank or the affiliate experienced financial difficulties, one would be tempted to, and sometimes did, act imprudently to preserve the stability and reputation of the other.").

[48] Banking (Glass-Steagall) Act of 1933, Pub. L. No. 73-66, 48 Stat. 162 (codified in scattered sections of 12 U.S.C.).

[49] Wade, *supra* note 7, at 372 (citing S. REP. NO. 73-77, at 6, 8, 10 (1933)).

[50] *Id.* (citing S. REP. NO. 73-1455, at 185 (1934)).

[51] The bank common trusts had "suffered fairly significant losses during the early Depression years. An SEC survey of 16 common trust funds indicated that the funds experienced an aggregate capital loss on total investments of approximately 18% during the period 1927-35, with the most severe declines occurring during the period 1930-32." *Id.* at 365 (citing SEC. & EXCH. COMM'N, COMMINGLED OR COMMON TRUST FUNDS ADMINISTERED BY BANKS AND TRUST COMPANIES, H.R. DOC. NO. 76-476, at 20 n.52 (1939)).

[52] Pub. L. No. 73-22, 48 Stat. 74 (codified as amended at 15 U.S.C. § 77a *et seq.*).

[53] Pub. L. No. 76-768, 54 Stat. 789 (codified as amended at 15 U.S.C. §§ 80a-1–80a-64 (2022)).

imposition of penalties for fraud or misrepresentation in the disclosure process. From the outset, the SEC considered a participating interest in a "common trust" fund to be a "security," which was defined under the Act to include any "investment contract."[54] However, the Act provided an exemption from the registration requirements for securities involved in a transaction "by an issuer not involving a public offering."[55] The SEC considered this exemption to be available to interests in common trust funds.[56]

In 1940, Congress passed the Investment Company Act ("ICA"). Congressional action had been spurred by an SEC study[57] conducted during the latter half of the 1930s, which focused on "investment trusts" established by bank security affiliates and functionally equivalent "investment companies" sponsored both by commercial and investment banking concerns.[58] The study revealed that investment trusts and investment companies were often used to promote the welfare of the sponsoring institutions to the detriment of investors.[59] In response, the ICA promulgated specific requirements regulating management structure, capital requirements, accounting processes, and sales practices of *investment companies*.

Importantly, in the period when the ICA was being considered, common trust funds were recognized as investment vehicles similar to investment companies.[60] However, common trust funds were still in their early stages and the SEC investigation of common trust funds was of "limited coverage" and did not attempt to study in detail possible abuses or defects involving such funds.[61] Accordingly, the ICA excluded "common trusts" from the definition of an "investment company."[62] The exclusion likely included the fact that common trust fund interests could not be merchandized as investments to the general public and that common trust funds themselves and their sponsoring banks were already subject to supervision and regulation by the Federal Reserve Board.[63]

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[54] *Id.*

[55] Securities Act § 4(2).

[56] Wade, *supra* note 7, at 378.

[57] *Id.* at 376 (citing SEC, Investment Trusts and Investment Companies, 75th-77th Cong. (1938-41)).

[58] *Id.*

[59] *Id.*

[60] *Id.*

[61] *Id.*

[62] *Id.* Specifically, Section 3(c)(3) of ICA excludes "any common trust fund or similar fund maintained by a bank exclusively for the collective investment and reinvestment of moneys contributed thereto by the bank in its capacity as a trustee, executor, administrator, or guardian . . . ." Investment Company Act of 1940, § 3(c)(3), 15 U.S.C. § 80a–3(c)(3).

[63] Wade, *supra* note 7, at 377.

2. The Growth of Pooled Bank Trusts for Pension Plans & the Ensuing Interagency Conflict: 1950s–1970s

The spate of legislative developments in the 1930s largely left the oversight of bank-sponsored common trusts to the Federal Reserve Board. By the 1950s, common trust funds were a "firmly established fiduciary banking practice" but still relatively small.[64] Developments in pension law would soon transform the fate and future of such trusts.

In the post WWII era, many U.S. companies established employer-sponsored retirement plans. Such plans were tax-qualified employee benefit plans that were structured as defined-benefit or traditional pensions. In other words, employers promised employees a certain monthly pension benefit upon retirement (and the satisfaction of vesting conditions), and employers bore the investment and longevity risks associated with such pension programs.

In 1955, the Federal Reserve Board authorized the establishment of pooled investment funds, which permitted, for the first time, the pooling of retirement trusts for investment purposes.[65] In what came to be an important development for CITs, the Board did not subject the pooled investment funds to the restrictions preventing the use of common trust funds primarily as investment vehicles.[66] The SEC then took two consequential positions: first, that pooled investment funds (i.e. the CITs) would not be considered investment companies under the ICA;[67] and second, that although an interest in a pooled investment fund would be considered a "security," the SEC would not impose the registration requirements on the assumption that transactions in pooled fund interests did not involve a "public offering."[68] These positions and the agency's "hands off" approach likely reflected "policy considerations relating to encouragement of pension plan growth, reliance on the ability of corporate plan sponsors to

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[64] *Id.* at 365.

[65] 12 C.F.R. § 206.10(c) (1955). To participate in a pooled investment fund, a trust had to "form part of a pension, profit-sharing, or stock bonus plan of an employer for the exclusive benefit of his employees or their beneficiaries and . . . [be] exempt from Federal income taxes under the Internal Revenue Code," and the governing instrument establishing the trust had to specifically authorize collective investment of its funds. *Id.*

[66] Wade, *supra* note 7, at 377. In addition to the "true fiduciary purpose" requirement discussed earlier, common trust funds were not to be advertised as investment vehicles. Moreover, individual account participations were limited to $100,000 or less, a limit that was the final "vestige of the original Federal Reserve Board policy that common trust funds be used primarily to aid in the administration of small fiduciary accounts." *Id.*

[67] The SEC determined at the time that section 3(c)(13) of the Act (predecessor to current section 3(c)(11)), which excluded "any employees' stock bonus, pension, or profit-sharing trust which meets the conditions of section 165 (now section 401) of the Internal Revenue Code" from the definition of "investment company," also extended to pooled investment funds. *Id.* (citing Robert H. Mundheim & Gordon D. Henderson, *Applicability of the Federal Securities Laws to Pension and Profit-Sharing Plans*, 29 LAW & CONTEMP. PROBS. 795, 834 (1964))

[68] The antifraud provisions of the Securities Act were thought still to apply. *Id.*

fend for themselves in the marketplace, and avoidance of overlapping jurisdiction between bank regulators and the SEC."[69] Following these regulatory developments, bank-sponsored pooled investment funds for retirement assets—that is, CITs—grew at a dramatic rate.[70]

The growth of CITs, now flush with retirement plan money—and certain regulatory developments in the 1960s—sparked pushback from the securities industry and a broader debate about the different regulatory regimes for CITs and mutual funds. The debate came to a head in 1962, when Congress allowed a new kind of tax-qualified retirement trust for self-employed individuals (referred to as H.R.-10 or Keogh plan trusts).[71] These plans removed the employer intermediaries that traditionally stood between individuals and retirement plan investments. The banking industry viewed these new individual plans as an exciting opportunity that, with appropriate advertising, could reach "potentially huge investor markets."[72]

The SEC and the securities industry took a less favorable view of these developments and suggested that some of its earlier justifications for a "hands off" approach would no longer apply. At Congressional hearings in 1963 and 1966, the SEC asserted that distribution of interests in pooled funds for H.R.-10 plan trusts involved a public offering of securities requiring registration under the Securities Act.[73] Notably, the SEC's position reflected concerns that a large number of relatively unsophisticated investors would have "neither the protective disclosure requirements of the Securities Act, nor the individualized, personal contact generally viewed as an integral part of traditional fiduciary services, to rely on."[74]

The SEC's position provoked strong disagreement from the OCC, which had been given supervisory authority over the trust powers of national banks from the Federal Reserve Board.[75] The Comptroller maintained that "the inspection and regulation conducted by the banking agencies was more than adequate to protect investors."[76]

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[69] Mundheim & Henderson, *supra* note 67, at 834.

[70] Frank L. Voorheis, *Investment Policy and Performance of Bank-Administered Pooled Equity Funds for Employee Benefit Plans,* 22 J. FIN. 492 (1967).

[71] Self-Employed Individuals Tax Retirement Act of 1962, Pub. L. No. 87-792, 76 Stat. 809 (codified in scattered sections of the Internal Revenue Code).

[72] Wade, *supra* note 7, at 366.

[73] U.S. SEC. & EXCH. COMM'N, PROTECTING INVESTORS: A HALF CENTURY OF INVESTMENT COMPANY REGULATION (1992).

[74] *Id.*

[75] The Comptroller then promulgated new regulatory guidance, which further loosened restrictions on CITs by eliminating the "true fiduciary purpose" requirement for accounts participating in common trust funds and authorizing the establishment of collective investment funds for managing agency accounts. 12 C.F.R. pt. 9; 28 Fed. Reg. 1111 (Jan. 31, 1963).

[76] Webb, *supra* note 36, at 343.

Over the next two decades, the dispute between the banking and securities industries, and their government regulators, produced Congressional hearings, litigation,[77] and legislation.[78] Although the Supreme Court in *Investment Co. Institute v. Camp* limited the banks' ability to operate certain investment funds open to the general public, and Congress clarified that CITs pooling HR-10 plans could not avail themselves of the all the securities law exemptions available to other CITs, the banks were otherwise permitted to continue their growing collective trust business.

Still, the securities industry continued its "vigorous campaign to secure legislation restricting the scope of bank activities."[79] In 1979, the Investment Company Institute (ICI) distributed to members of Congress a publication entitled "Misadventures in Banking: Bank Promotions of Pooled Investment Funds."[80] In the report, the ICI argued that "[t]he operation of bank pooled investment funds solely to provide investment management services for retirement plans constitutes a clear violation of the Glass-Steagall Act."[81] The ICI insisted that the interests in pooled funds are considered securities for securities law purposes and that by marketing these interests aggressively to employee benefit funds, banks were actively competing in the investment banking business and thus violating the Glass-Steagall Act and the guidance in *Camp*.[82] The ICI asked Congress to "make it clear that commercial banks and their affiliates are totally prohibited from sponsoring, organizing, controlling and advising every type of pooled investment fund other than traditional bank common trust funds."[83]

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[77] Inv. Co. Inst. v. Camp, 401 U.S. 617 (1971). The case, which "involve[d] a double-barreled assault upon the efforts of a national bank to go into the business of operating a mutual investment fund" and which ultimately reached the Supreme Court in 1971, clarified that the Glass-Steagall Act prohibits a commercial bank from performing an "underwriting" function in the offering of an investment management service, such that the bank may not sell investments (but can offer fiduciary services). In other words, the Glass-Steagall Act prohibits national banks from operating investment funds that offer customers opportunities to invest in stock funds created and maintained by banks. Wade, *supra* note 7, at 395.

[78] The Investment Company Amendments Act of 1970 clarified that interests in bank trusts used to fund employee pension plans, other than the H.R. 10 self-employed plans, are exempted from the registration provisions of both the 1933 and the 1934 Acts. Interests in collective H.R. 10 plans are similarly exempted as to the 1934 Act, but not as to the 1933 Act, except as the Commission may provide otherwise by rule or order. Congress also amended the ICA to clarify that any employee's stock bonus, pension, or profit-sharing trust which meets the requirements for qualification under section 401 of the Internal Revenue Code would not be considered an investment company subject to ICA rules, nor would any collective trust fund maintained by a bank consisting solely of the assets of such trusts. Investment Company Amendments Act of 1970, Pub. L. No. 91-547, 84 Stat. 1413 (codified in scattered sections of 15 U.S.C.).

[79] Wade, *supra* note 7, at 395.

[80] *Id.* at 395 n.193.

[81] *Id.*

[82] *Id.*

[83] *Id.*

Despite such pushback from the securities industry, and various efforts to resolve the difficult questions of law and policy raised by increasing bank involvement in investment management activities, the questions remained largely unanswered, and the regulatory framework for CITs remained unchanged. Ultimately, as discussed further in Section II.A.4, the securities industry decided to take the "if you can't beat them, join them" approach. Rather than continuing to try to fight bank activity in the CIT space, asset managers simply decided to set up banks and trust companies to offer their own CITs.

3. The New Era of Defined Contribution Retirement Plans (1980s to Present)

Whereas the bulk of retirement plans established in the post WWII period were traditional "defined benefit" plans, starting in the 1980s, employers began to shift to "defined contribution" plans for their employees.[84] The change came after Congress created the 401(k) plan, now the most common type of defined contribution plan, by amending section 401 of the Code in 1978.[85]

Defined contribution plans differ from defined benefit plans in several respects. In a defined benefit plan, employers promise the employees a specific monthly benefit payable from retirement until death. Employers also choose and manage the plans' investments and bear any investment risk associated with the plans. Furthermore, the Employee Retirement Income Security Act of 1974 (ERISA), the law that governs private-sector retirement plans in the United States, was drafted specifically for defined benefit plans and imposed numerous substantive requirements to protect the interests of plan participants.[86]

In a defined contribution plan, an employer promises only to make a specified contribution to an individual account for each employee's benefit. Therefore, an employee's benefits in retirement are not fixed, but depend on the contributions made to the individual account, as well as the investment performance of the assets in that account. An employee in a defined contribution plan will ultimately receive the nonforfeitable accrued balance in the employee's account, which is based on contributions plus or minus investment gains or losses.

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[84] U.S. SEC. & EXCH. COMM'N, *supra* note 73; *see also* Alicia Munnell, *Private Sector Defined Benefit Plans Are Really Disappearing*, CTR. FOR RET. RSCH. AT B.C. (Dec. 26, 2011), https://crr.bc.edu/private-sector-defined-benefit-plans-are-really-disappearing/ [https://perma.cc/37L2-9BHH] (observing the decline of defined benefit plans in the private sector).

[85] The amendment exempted from taxation certain profit-sharing and stock bonus plans that allowed employees to elect either to receive or defer receipt of a portion of their compensation. If the employee elected to defer receipt of the contribution, it would be invested in a trust. The contributions and the earnings would then accumulate tax-free until disbursed. Revenue Act of 1978, Pub. L. No. 95-600, § 135, 92 Stat. 2763, 2785 (codified as amended at 26 U.S.C. § 401(k) (2022)).

[86] Employee Retirement Income Security Act (ERISA) of 1974, Pub. L. No. 93-406, 88 Stat. 829 (codified as amended in scattered sections of 29 U.S.C. and 26 U.S.C.). *See generally* Natalya Shnitser, *Trusts No More: Rethinking the Regulation of Retirement Savings in the United States*, 2016 BYU L. REV. 629 (describing the aims of and key requirements under ERISA).

Defined-contribution plans require employee participants to select investments for their individual accounts from a menu of options curated by the plan sponsor. In so doing, defined contribution plans shift the investment management risk and responsibility onto individual employees. Plan administrators are subject to fiduciary obligations and must choose prudently and monitor the investment options available to participants, but they have no obligation to ensure that participants choose suitable investments from the available options.

The shift to defined contribution plans prompted regulators to reconsider the disparate treatment of mutual funds and CITs, and to question whether the securities laws exemptions were still justified given the changing retirement plan landscape. In a 1992 report, the SEC Division of Investment Management observed that changes in the U.S. retirement system "eviscerate[d] the original rationale for the exemptions from securities disclosure requirements for pooled investment vehicles—that large employers, making the investment decisions and bearing the investment risks, could obtain needed information without disclosure requirements."[87] The SEC rejected the argument that changes to the securities law exemptions were unnecessary given federal laws and regulations already applicable to retirement plans and CITs. Specifically, because ERISA disclosure requirements focused primarily on the "plan itself and not on the investments that underlie the plans," participants in plans that included CITs on their investment menus would have access to less information than participants in plans with mutual funds on the menu.[88] Moreover, the SEC maintained the position that existing bank regulation was not a substitute for the investor protections of the federal securities laws because "banking regulation was concerned primarily with controlling the flow of credit, maintaining an effective banking structure, and protecting depositors. Banking regulation does not address investors' need for information.[89]

Based on its analysis, in 1992 the Division of Investment Management made recommendations that would bifurcate the securities law treatment for CITs based on whether the CIT held defined-benefit or defined-contribution plans assets. Specifically, the Division recommended that the Commission send to Congress legislation that would: (1) remove the exemption from registration in section 3(a)(2) of the Securities Act of 1933 for interests in pooled investment vehicles for participant-directed defined contribution plans; (2) amend the federal securities laws to require the delivery of prospectuses for the underlying investment vehicles to plan participants who direct their investments; and (3) amend the Securities Exchange Act of 1934 to require the delivery of semiannual and annual shareholder reports for the underlying investment vehicles

[87] U.S. SEC. & EXCH. COMM'N, *supra* note 73, at 144.
[88] *Id.* at 146.
[89] *Id.* at 128.

(other than registered investment companies) to plan participants. For defined benefit plan assets and defined contribution plans that do not provide for participant direction, the Division recommended retaining the current Securities Act exemptions in their current form.

Although the SEC was not the only agency in favor of reform to the laws governing CITs, no major changes to the regulatory framework for CITs were enacted.[90] Instead, the SEC,[91] the DOL[92] and the OCC[93] all promulgated regulatory guidance that further integrated CITs into the existing financial ecosystem. Still, because CITs lacked the familiarity and operational ease of mutual funds, plan sponsors were somewhat reluctant to embrace them as a substitute. The next two decades would see industry efforts to eliminate some of the barriers to adoption of CITs and, correspondingly, both greater convergence and competition with mutual funds.

4. Intensifying Convergence and Competition with Mutual Funds: 2000 to the Present

Since 2000, CITs have pushed to eliminate or minimize "the historical disadvantages" and barriers to adoption.[94] Together with the pressure on plan sponsors to avoid litigation over plans fees, there has been "a perfect storm"[95] of forces in favor of CITs. As noted earlier, the exodus out of mutual funds has accelerated in recent years and appears to be reaching all segments of the retirement plan market, including smaller plans that did not previously have CITs on their investment menus.

Four key developments have made CITs more appealing to plan sponsors. First, in 2000, the National Securities Clearing Corporation (NSCC) added CITs to its mutual fund trading platform.[96] While mutual funds remain more

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[90] As part of its proposal to "modernize" the financial system, the Department of the Treasury recommended "regulating banks' pooled investment activities in a manner more similar to investment companies." *See* U.S. DEP'T OF THE TREASURY, MODERNIZING THE FINANCIAL SYSTEM 59 (1991).

[91] In 1981, the SEC adopted Rule 180, which exempts an interest in a Keogh plan, and the plan's interest in a pooled investment vehicle, from Securities Act registration on the basis of the financial and business sophistication of the employer or on the employer's solicitation of advice from an independent expert. Exemption from Registration of Interests and Participations Issued in Connection with Certain H.R. 10 Plans, 46 Fed. Reg. 58,291, (Nov. 24, 1981) (to be codified at 17 C.F.R. § 230.180).

[92] In 1991, the DOL adopted Prohibited Transaction Class Exemption 91-38, specifically providing certain exemptions for CITs and their trustees/managers.

[93] In 1997, the OCC revised and updated the rules governing commingled funds, including CITs. *See* FED. DEPOSIT INS. CORP., TRUST EXAMINATION MANUAL § 7(2005), https://www.fdic.gov/regulations/examinations/trustmanual/section_7/section_vii.html [https://perma.cc/6DB7-54ZD].

[94] DESAI & DAUWEN, *supra* note 7, at 5. The change streamlines the purchase, redemption, and exchange transactions and allows investors to access real-time information about contributions, distributions and other activities.

[95] *Id.*

[96] *Id.*

transparent than CITs, in recent years, database vendors such as Morningstar, who closely track mutual funds, have expanded their coverage of CITs. Some industry estimates suggest that Morningstar currently covers upwards of 95% of the CITs being offered, although Morningstar itself provides no such estimates and does not have information about the number of CITs not in its database.[97] Although CITs, unlike mutual funds, have no regulatory obligation to provide daily pricing to investors, increasingly, more and more asset managers provide daily pricing.[98]

At the same time, plan sponsor demand for CITs has also increased. The increased demand is a function of several regulatory, litigation, and market developments, some of which have played out in tandem over the last two decades. In 2006, the Pension Protection Act required retirement plan sponsors to invest uncommitted 401(k) dollars—that is, contributions for which participants had not specified an investment preference—automatically into so-called "Qualified Default Investment Alternatives." QDIAs came to be dominated by Target Date Funds (TDFs), which offer in a single fund a mix of stocks, bonds, and short-term investments, the balance of which is adjusted automatically based on the investor's age. The ability of CITs to hold different kind of securities has made CITs particularly well-suited for the TDF space. Both the use of TDFs, and TDFs structured as CITs has grown dramatically over the last fifteen years.[99]

Just as plan sponsors were adjusting to the QDIA requirements, the DOL also finalized several rules to improve fee disclosure and facilitate comparison across retirement plan investment options. In particular, in its 2012 rule, the DOL sought to "ensure that employee benefit plan fiduciaries, as well as plan participants and beneficiaries, obtain comprehensive information about the services that are provided to employee benefit plans, and the cost of those services. [100] The DOL rule set forth the disclosures that must be furnished to plan fiduciaries in order for a contract or arrangement for plan services to be "reasonable," as required by ERISA. The rule enhanced and standardized the information that

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[97] *Id.* at 12. Morningstar indicates that "CITs (as all other funds) are added to our database at the request of fund companies and/or at the request of third-party clients with the fund company's permission. We do not have access to the CITs (or the number of CITs) that are not included in our database." Email from Morningstar Direct (on file with author).

[98] One industry report suggests that the vast majority of CITs trade and price daily. *See* COAL. OF COLLECTIVE INV., TRS.., COLLECTIVE INVESTMENT TRUSTS (2021), https://www.seic.com/sites/default/files/2022-05/SEI-STC-CCIT-WhitePaper.pdf [https://perma.cc/6V8K-CCYD]

[99] According to Morningstar, "target-date strategies raked in $153 billion in net assets in 2022; collective investment trusts led the way, absorbing $121 billion—or 79%—of the year's net inflows. CITs make up 47% of target-date strategy assets as of the end of 2022 and are projected to become the most popular target-date vehicle within the next two years." *See* MORNINGSTAR, TARGET-DATE STRATEGY LANDSCAPE: 2023 (2023).

[100] Reasonable Contract or Arrangement Under Section 408(b)(2)–Fee Disclosure, 77 Fed. Reg. 5632 (July 1, 2012) (to be codified at 29 C.F.R. pt. 2550).

financial institutions, including those managing CITs, would have to provide to plan administrators, thereby reducing some of the disclosure gaps between CITs and mutual funds.

The last, and arguably the most significant, driver of the shift to CITs has been ERISA litigation. Specifically, over the last fifteen years, retirement plan sponsors—and the individuals deemed to be ERISA fiduciaries—have faced heightened litigation risk over their administration and management of company retirement plans. The bulk of such lawsuits, which name as defendants not only the plan sponsors but also the individual fiduciaries who serve on plan committees during the relevant time periods, have been "excessive fee" cases focused specifically on the selection of service providers and investment options for the plan. Plaintiffs have repeatedly challenged the selection and retention of allegedly overpriced and underperforming investments.[101]

The volume of both the lawsuits and the settlement amounts has drawn the attention and the concern of industry groups, who have sought to underscore the legal exposure of those associated with ERISA plans, and the significant increases in the fiduciary insurance costs.[102] CITs have emerged—and have been marketed[103]—as a direct response to concerns about fee litigation, while also offering greater flexibility on the use alternative investments in retirement plans.[104] As Section IV shows, however, while CITs satisfy some of the concerns raised by plaintiffs in the "excessive fee" cases, the use of CITs also makes further monitoring of retirement plan menus by plaintiffs' attorneys considerably more difficult.

B. The Current State of the CIT Market

While there is no single source of information on the size and characteristics of the CIT market, data from the Department of Labor (DOL) and from

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[101] Shnitser, *supra* note 24.

[102] *Id.*; SOMPO INT'L, ERISA & EXCESSIVE FEE LITIGATION BY THE NUMBERS (2023) (suggesting that total damages from excessive fee litigation between 2010 and 2022 exceed $1 billion); CHUBB, EXCESSIVE LITIGATION OVER EXCESSIVE PLAN FEES (2021), https://www.chubb.com/content/dam/chubb-sites/chubb-com/us-en/business-insurance/fiduciary-liability-educational-materials/documents/pdf/2021-09-15_Excessive_Litigation_over_Excessive_Fees.pdf [https://perma.cc/YE4W-TWGX] (reporting that "the average excessive fee settlement was approximately $14.5 million in 2020").

[103] *See, e.g.*, JENNIFER DELONG, ALLIANCEBERNSTEIN, WHAT'S OLD IS NEW AGAIN: COLLECTIVE INVESTMENT TRUSTS REDUCE DC PLAN COSTS i (2020), https://www.alliancebernstein.com/content/dam/global/insights/insights-whitepapers/OldAreNewAgain.pdf [https://perma.cc/Y9MH-43S2] ("With more scrutiny on plan fees recently and a big surge in litigation, CITs are a transparent and lower-cost option for plan sponsors.").

[104] Unlike mutual funds subject to the ICA, CITs have much more leeway to invest in alternatives like TIPS, real estate, commodities, high-yield bonds and hedge funds. The CIT structure also permits fixed and indexed annuities to be incorporated in certain target date funds for "timing optimal cash flow during the required minimum distribution (RMD) phase." DESAI & DAUWEN, *supra* note 7, at 21.

the Morningstar Direct database sheds light on the prevalence of CITs in employer-sponsored plans as well as on largest managers of CIT assets. The DOL reports that as of 2021, there were 95,028 private-sector retirement plans with 100 or more participants, including 6,715 defined benefit plans and 88,313 defined contribution plans.[105] Of these, 30,540 had assets invested in one or more of the 5,088 collective investment trusts, which in the aggregate held over $4.6 trillion dollars.[106] Of the total assets, more than half ($2.5 trillion) was held in common stock, while the rest was distributed across a variety of other investments. Morningstar Direct data is consistent with these findings and Table 1 of the Appendix shows the distribution of CITs investment strategies. While a variety of investment strategies—including commodities and alternatives—is represented, nearly two thirds of CIT assets are invested in target date or U.S. equities.

Who manages the CIT assets across the various investment strategies? Table 1 below draws on data in the Morningstar Direct database to compile the ten largest CIT managers. At the very top are BlackRock and Vanguard, each with over a trillion dollars in CIT assets under management. T. Rowe Price and State Street follow, each with over $400 billion in CIT assets. Fidelity rounds out the top five, managing nearly $200 billion in CIT assets. Table 1 shows that the "Big Three" asset managers have extensive CIT business lines. Section II.C below describes the different organizational structures used to offer CITs to retirement plan clients.

Table 1: Top Ten CIT Managers by Total Assets as of 2023[107]

	Total Net Assets ($Bil) as of 2023	**2023 Market Share (%)**
BlackRock (including managers identified as "BlackRock Institutional Trust Company NA," "BlackRock," "Blackrock, Inc." and "BlackRock Fund Advisors"	1,069	22.57
Vanguard Group Inc	1,060	22.39

105 EMP. BENEFITS SEC. ADMIN., U.S. DEP'T OF LAB., PRIVATE PENSION PLAN BULLETIN HISTORICAL TABLES AND GRAPHS 1975-2021 (2023), https://www.dol.gov/sites/dolgov/files/ebsa/researchers/statistics/retirement-bulletins/private-pension-plan-bulletin-historical-tables-and-graphs.pdf. The DOL reports cover only private-sector plans subject to its regulatory oversight.

106 EMP. BENEFITS SEC. ADMIN., U.S. DEP'T OF LAB., FORM 5500 DIRECT FILING ENTITY BULLETIN: ABSTRACT OF 2021 FORM 5500 ANNUAL REPORTS (2023), https://www.dol.gov/sites/dolgov/files/ebsa/researchers/statistics/retirement-bulletins/form-5500-direct-filing-entity-bulletin-abstract-of-form-5500-2021-preliminary-annual-report.pdf [https://perma.cc/JS7P-UZEP].

107 Data in this table is from the Morningstar Direct list of the twenty largest CIT managers ranked by total assets. Within that list, Table 1 combines managers by name as described above.

T. Rowe Price (including managers identified as "T. Rowe Price" and "T. Rowe Price Associates, Inc.")	486	10.27
State Street Global Advisors	434	9.17
Fidelity (including managers identified as "Fidelity Institutional Asset Management," "Fidelity Management & Research Company LLC" and "Fidelity Management Trust Company"	314	6.64
Geode Capital Management, LLC	139	2.94
Mellon Investments Corporation	136	2.87
JPMorgan Chase Bank, N.A.	104	2.19
MissionSquare Retirement	74	1.57
Principal Global Investors Trust Company	55	1.16
Total	**3,872**	**81.77**

C. CIT Organization, Governance, and Oversight

In examining the organization, governance and oversight of CITs, it is helpful to start with an example showing how CITs describe themselves. The following excerpt comes from a BlackRock CIT fact sheet (emphasis added):

> The fund described herein is a bank-maintained collective investment fund **maintained and managed** by BlackRock Institutional Trust Company, N.A. ("BTC"). BTC is a **national banking association** organized under the laws of the United States and operates as a limited purpose trust company. In reliance upon an **exemption from the registration requirements of the federal securities laws**, investments in the fund are not registered with the Securities and Exchange Commission ("SEC") or any state securities commission. Likewise, in reliance upon an **exclusion from the definition of an investment company in the Investment Company Act of 1940**, as amended (the "Company Act"); the fund is not registered with the SEC as an investment company under the Company Act. The **Office of the Comptroller of the Currency** is responsible for ensuring that fiduciary powers are exercised in a manner consistent with the best interests of BTC's clients and sound fiduciary principles.
>
> The fund is offered to defined contribution plans ("Plans") that are qualified under Section 401(a) of the Internal Revenue Code of 1986, as amended ("IRC"), and governmental Plans, such as state and municipal government Plans that are described in IRC Section 818(a)(6), such as governmental IRC Section 457(b) Plans. The fund is established and governed by a trust instrument, the Plan of BlackRock

> Institutional Trust Company, N.A. Investment Funds for Employee Benefit Trusts (the "Plan Document"), which sets forth BTC's powers, authority and responsibilities regarding the administration, investment and operation of the fund. Plans investing in the fund become subject to the terms and conditions of the Plan Document.[108]

While BlackRock relies on a national banking association, other CIT providers are organized differently. Vanguard CITs are maintained by the Vanguard Fiduciary Trust Company, a Pennsylvania non-depository trust company that is a wholly owned subsidiary of The Vanguard Group, Inc.[109] In 2016, State Street Bank and Trust Company established State Street Global Advisors Trust Company (SSGA Trust), a limited purpose trust company operating pursuant to the laws of the Commonwealth of Massachusetts.[110] The T. Rowe Price Collective Investment Trusts are established by T. Rowe Price Trust Company under Maryland banking law.[111] Fidelity CITs, meanwhile, are maintained by the Fidelity Institutional Asset Management Trust Company, a trust company organized under the laws of the state of New Hampshire.[112]

The organization, governance, and oversight of CITs is unique and differs in material ways from that of mutual funds. Table 2 below summarizes the key differences, and the paragraphs that follow describe the differences in more detail. The regulatory structure is important both for its impact of retirement savings and the U.S. capital markets, and because it is directly tied to the "cost savings" and "greater flexibility" that CITs claim to offer to retirement plans. Indeed, industry participants have identified "regulatory risk"— that is, "unforeseen regulatory challenges and documentation requirements at the hands of regulators"—as the biggest risk to the market opportunity for CITs.[113]

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[108] *BlackRock Equity Index Fund J*, Morningstar, Inc., Morningstar Investment Profiles (on file with author). The CIT trustee and manager may or may not be the same entity. In general, the trustee selects the manager or sub-advisor for the CIT.

[109] *Target-Date Funds*, VANGUARD, https://institutional.vanguard.com/investment/solutions/target-date-funds.html [https://perma.cc/H4FF-JU8L]. The Vanguard Fiduciary Trust Company was founded in 1981. *Serving Investors for Nearly Five Decades*, VANGUARD, https://corporate.vanguard.com/content/corporatesite/us/en/corp/who-we-are/sets-us-apart/our-history.html [https://perma.cc/HBB9-SKEX].

[110] *Establishment of State Street Global Advisors Trust Company a Limited Purpose Trust Company by State Street Bank and Trust Company*, MASS.GOV (Sept. 23, 2016), https://www.mass.gov/decision/establishment-of-state-street-global-advisors-trust-company-a-limited-purpose-trust-company-by-state-street-bank-and-trust-company [https://perma.cc/CK9M-DZ5A].

[111] Since 1984, T. Rowe Price Trust Company has offered CITs "to provide institutional investors an attractive alternative to mutual funds and separate accounts." T. ROWE PRICE, THE ADVANTAGES OF T. ROWE PRICE COLLECTIVE INVESTMENT TRUSTS (2023), https://www.troweprice.com/content/dam/fai/Investments/CIT/literature/cit-brochure.pdf [https://perma.cc/4FEA-76LP].

[112] *Fidelity Freedom Plus Commingled Pools*, FIDELITY, https://institutional.fidelity.com/app/item/RD_9907809/freedom-plus-strategy.html [https://perma.cc/LP7B-7E24].

[113] DESAI & DAUWEN, *supra* note 7, at 25.

Table 2: Mutual Funds vs. CITs

	Collective Investment Trusts	**Mutual Funds**
Type of investment vehicle	Pooled The trusts are established by banks or trust companies	Pooled The funds are set up as separate entities by management companies
Governance Structure	CITs are controlled by banks, which must have "exclusive management" of the CIT, although banks may engage subadvisors, so long as the banks retain final decision-making authority.[114] No governance role for individual investors or retirement plan sponsors	Management companies provide asset management for the fund Under the ICA, fund shareholders elect mutual fund directors and vote on certain governance matters for the fund
Who can invest?	Qualified retirement plans only; not available to individual investors	All investors
Fee Structure	Custom fee structures negotiated with retirement plan sponsor	Set by asset manager and disclosed in the prospectus
Permissible Investments	No regulatory limits on the amount or percentage of illiquid or alternative assets; can hold real estate, timber, private equity interests, among others	Restrictions on certain types of assets
Governing Documents	Declaration of Trust	Prospectus and additional filings
Advertising / Materials	Advertising not allowed	Prospectus and various literature
Trading	Most can trade via NSCC	NSCC trading
Valuation	Daily valuation not required; OCC requires valuation at least quarterly	Daily valuation
Admissions & Withdrawals	Daily purchases and sales of interests not required; must be specified in written plan	Daily purchases and sales
Financial Reporting	Audited Financial Statements Form 5500 optional, but usually filed by trustee	Annual report Form 5500 required
Proxy Vote Reporting	Not required	Required by SEC
Portability	Must be liquidated to rollover	Possible to rollover seamlessly
Oversight & Regulation	Office of the Comptroller of Currency (OCC) and DOL Fund trustee subject to ERISA standards if underlying retirement plan subject to ERISA CITs are typically structured to avoid registration with the SEC	SEC Manager not held to ERISA standards

As Table 1 shows, the regulatory framework for CITs is both complex and fractured. The following parts review the regulatory structure by addressing each of the relevant regulatory agencies in turn.

[114] 12 C.F.R. § 9.18(b)(2) (2022).

1. State and Federal Banking Regulators

CITs established by national banks or trust companies fall under OCC oversight. CITs sponsored by state-chartered institutions, meanwhile, are subject to oversight by state regulators. At the outset then, the regulatory framework for CITs is not uniform.[115] For CITs established by national banks, the bank acts as a fiduciary for the fund and holds legal title to the fund's assets.[116] Participants are the beneficial owners of the fund's assets. As the OCC notes, "[w]hile each participant owns an undivided interest in the aggregate assets of a CIF, a participant does not directly own any specific asset held by a CIF."[117] Participating interests in a CIT are not insured by the Federal Deposit Insurance Corporation and are not subject to potential claims by a bank's creditors.[118]

The OCC regulations spell out the key governance requirements for CITs. First, the OCC defines a CIT as "a fund consisting solely of assets of retirement, pension, profit sharing, stock bonus or other trusts that are exempt from Federal income tax."[119] In addition, the OCC regulations require, in key part, that the CIT be established pursuant to a written plan, that the bank sponsoring a CIT have "exclusive management" of the CIT, subject to prudent delegation; that the CIT be valued at least quarterly; that it produce a financial report at least annually; that management fees be "reasonable" and that the CIT complies with certain risk management requirements.[120] Notably, the regulations prohibit banks from advertising or publicizing CITs, "except in connection with the advertisement of the general fiduciary services of the bank."[121] As has been pointed out by other regulators and observers, the OCC is a bank regulator whose main concern is "ensuring a safe and sound federal banking system for all Americans."[122] Accordingly, both its regulatory provisions and its risk-management guidance are geared primarily to ensuring bank stability.

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115 Although state law dictates, many states rely on and borrow from OCC guidance. *See Recent SEC Enforcement Raises Questions for Bank Collective Trust Funds*, EVERSHEDS-SUTHERLAND (Oct. 6, 2020), https://us.eversheds-sutherland.com/NewsCommentary/Legal-Alerts/235939/Recent-SEC-enforcement-raises-questions-for-bank-collective-trust-funds [https://perma.cc/WAY6-462U] (noting that "many states apply the OCC's rules either by statute, rule, other guidance or as best practices in examining state bank collective trust activities").

116 The OCC uses the term "collective investment fund" to refer to CITs.

117 OFF. OF THE COMPTROLLER OF THE CURRENCY, COMPTROLLER'S HANDBOOK: ASSET MANAGEMENT: COLLECTIVE INVESTMENT FUNDS 1 (2014), https://www.occ.treas.gov/publications-and-resources/publications/comptrollers-handbook/files/collective-investment-funds/pub-ch-collective-investment.pdf [https://perma.cc/YNM3-2Y89].

118 *Id*.

119 Technically there are two types of collective funds: A1 funds are established under 12 C.F.R. § 9.18(a)(1), and A2 funds are established under 12 C.F.R. § 9.18(a)(2). Retirement plans participate in the latter.

120 12 C.F.R. § 9.18(b) (2022).

121 *Id*.

122 OFF. OF THE COMPTROLLER OF THE CURRENCY, https://www.occ.treas.gov/ [https://perma.cc/4GB4-SYUE].

2. The Department of Labor

The Department of Labor has oversight over entities and individuals that hold the assets of certain retirement plans covered by ERISA. Because CITs are deemed to hold ERISA "plan assets," the trustee and any sub-adviser of a CIT are considered ERISA fiduciaries and must comply with ERISA fiduciary duties in managing the CIT. Fiduciary duties include the duty of loyalty to plan participants, the duty of prudence, the duty of prudent diversification, and the duty to follow plan terms. Breaching fiduciary standards carries the risk of personal liability. Furthermore, under the so-called "prohibited transaction" rules, ERISA fiduciaries are prohibited from engaging in certain transactions with "parties in interest" (i.e., certain entities that are related to the plan or provide services to the plan or their affiliates).[123]

CIT sponsors are also subject to various reporting and disclosure requirements under ERISA, which aim to facilitate information sharing with plan sponsors, plan participants, and the Department of Labor.[124] In this regard, the Department of Labor generally treats CITs and mutual funds in the same way. The challenge, however, is that mutual funds are subject to considerably greater disclosure and reporting requirements under the securities laws. As described below, CITs are generally exempt from such requirements, thus greatly reducing the amount of publicly accessible information about CITs.

3. The Securities & Exchange Commission

The SEC's oversight over CITs is limited by a series of exemptions, which render most of the securities laws inapplicable to CITs. Typically, CITs are structured to comply with the requirements of Section 3(c)(11) of the Investment Company Act of 1940 to avoid being treated as an "investment company."[125] While CIT interests are considered "securities" under the Securities Act and the Securities Exchange Act (and subject to the general antifraud provisions under the Securities Act), they typically qualify for exemptions from

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[123] *See generally 29 CFR 2570 Prohibited Transaction Exemption Procedures Employee Benefit Plans*, EMP. BENEFITS SEC. ADMIN., U.S. DEP'T OF LAB., https://www.dol.gov/agencies/ebsa/laws-and-regulations/rules-and-regulations/exemptions/class/pte-procedures [https://perma.cc/X6P7-GB6F].

[124] These include service provider fee disclosures required under 29 C.F.R. § 2550.408b-2, and investment-related disclosures required under 29 C.F.R. § 2550.404a- for defined contribution plans. In addition, a CIT may, but is not required to, file a separate Form 5500 as a "direct filing entity."

[125] Investment Company Act of 1940, 15 U.S.C. § 80a-3(c)(11) (exempting "any employee's stock bonus, pension, or profit-sharing trust which meets the requirements for qualification under section 401 of the title 26, or any governmental plan described in section 77c(a)(2)(C) of this title; or any collective trust fund *maintained by a bank* consisting solely of assets of one or more of such trusts, government plans, or church plans, companies or accounts that are excluded from the definition of an investment company under paragraph (14) of this subsection").

registration requirements.[126] Key to these exemptions are the limitations on participating investors (i.e., certain retirement plans) and the requirement that the CITs be "maintained by a bank."[127]

Given these exemptions, CITs do not have to issue prospectuses which, for mutual funds, require the fund to disclose information on a fund's investment objective, portfolio managers, fees, services, restrictions, and policies, along with information related to risks, conflicts of interest, and other topics prescribed by the SEC. CITs may decide to offer "fact sheets" and must provide certain fee disclosures to plan sponsors (but not to the public) in connection with DOL requirements. CITs are also exempt from requirements to report performance and holdings on at least a semiannual basis, in a standardized manner, as well as to provide quarterly account statements to investors. As noted above, OCC-regulated CITs are only required to issue financial reports on an annual basis, although they may report more frequently. In sub-regulatory guidance, the SEC has further indicated that CITs should not be promoted as an investment vehicle for the public, and that there should be no television or radio advertising of CITs.[128]

Finally, because they are not "investment companies," CITs avoid all of the substantive regulation under the Investment Company Act, including regulation about fund governance and permissible investments. The ICA "requires mutual funds to give their shareholders a minimum set of control rights,"

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[126] Section 3(a)(2) of the Securities Act of 1933 generally excepts from registration the securities issued by collective trust funds. *See* 15 U.S.C. § 77c(a)(2) (exempting, in part, "any interest or participation in a single or collective trust fund *maintained by a bank* . . . which interest or participation is issued in connection with (A) a stock bonus, pension, or profit-sharing plan which meets the requirements for qualification under section 401 of the Internal Revenue Code of 1954). Section 3(a)(12) of the Securities Exchange Act of 1934 exempts the securities issued by these vehicles from the registration requirements of that Act. *See* 15 U.S.C. § 78c(a)(12).

[127] A "bank" is broadly defined in the ICA as any banking institution or trust company doing business under State or federal law, as long as "a substantial portion of the business of which consists of receiving deposits or exercising fiduciary powers similar to those permitted to national banks, and which is supervised and examined" by a State or Federal banking regulator and is not operated for the purpose of evading the 1940 Act. Accordingly, most banks and trust companies will satisfy the definition of "bank." *See* De Leon, *supra* note 2. A bank may hire a "subadvisor" or external advisor to assist it with managing the CIT, but the bank must retain final decision-making authority. *Id.* The use of subadvisors is quite common, as evidenced by the industry's pushback against proposed DOL regulatory guidance that could limit the practice. *See, e.g.*, Letter from Clifford Kirsch & Carol McClarnon, Coal. of Collective Inv. Trs., to Off. of Exemption Determinations, Emp. Benefits Sec. Admin., U.S. Dep't of Lab. (Mar. 31, 2023), https://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/public-comments/1210-ZA07-3/00002.pdf [https://perma.cc/X3WE-XA66] (arguing that the proposed amendment, which limited the exemption to transactions over which the QPAM exercised "sole responsibility" was inconsistent with the use of subadvisors by CIT QPAMs).

[128] De Leon, *supra* note 2 (first citing Huntington Nat'l Bank, SEC No-Action Letter, 1988 WL 234053 (Mar. 9, 1988); and then citing Nat'l Emp. Plan Servs., Inc., SEC No-Action Letter, 1984 WL 48398 (Oct. 16, 1984)).

including the right to elect the board of directors of the fund, and to terminate and replace the funds' management company.[129] In contrast, CIT investors have no management rights, and the decision-making authority rests entirely with the bank trustee. Furthermore, as SEC Chairman Gensler has lamented in recent months, whereas the SEC can and has proposed rules to update liquidity and pricing requirements for mutual funds, CITs are subject to none of those same requirements and the SEC lacks authority to impose them on "functionally similar" investment vehicles.[130]

4. The Internal Revenue Service

The tax treatment of CITs is integral to their appeal and growth. In 1936, Congress amended the Internal Revenue Code (IRC) to provide tax-exempt status to certain CITs maintained by banks. Today, to maintain tax-exempt status, a CIT holding retirement plan assets will typically seek to qualify as a group trust pursuant to Revenue Rulings 81-100 and 2011-1, and IRC section 401(a). Most importantly, each account participating in the CIT either must qualify as a tax-exempt entity under section 401(a) of the IRC or be an entity described in section 818(a)(6) of the IRC. Similarly, as noted above, interests in CITs will qualify as "exempt securities" under Section 3(a)(2) of the Securities Act so long as participation in the fund is limited to certain types of investors, such as a pension or profit-sharing plan qualified under Internal Revenue Code Section 401(a), or a governmental plan as defined in Internal Revenue Code Section 414(d). For this reason, retirement plans of non-profits and higher education institutions, for example, which are "qualified" under Section 403(3)(b) of the IRC (rather than 401(k)), currently cannot participate in CITs.

5. Regulatory Crossroads & the Functional Regulation Debate

The discussion in this section shows that CITs exist at the intersection of—or perhaps in the chasm between—multiple academic and regulatory fields. They are retirement "products" set up and run by banks and trust companies, with regulatory oversight from both the Office of the Comptroller of the Currency and the Department of Labor. Since CITs are only available to qualified retirement plans, they have not been studied by banking scholars. And as bank-run funds under OCC oversight, they have not garnered much attention from employee benefits scholars. While such regulatory fragmentation may be appealing to industry participants, it has hampered academic research on CITs in

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[129] John D. Morley, *The Separation of Funds and Managers: A Theory of Investment Fund Structure and Regulation*, 123 YALE L.J. 1228, 1252 (2014).

[130] Gensler, *supra* note 4 (expressing concern about "financial fires" starting from "regulatory gaps" and noting that the SEC is "in discussions with the bank regulators on these topics").

recent years, including both targeted analyses of CITs and more theoretical considerations of "functional" regulation.

Mutual funds and CITs are functionally similar and serve similar purposes in today's financial ecosystem. Yet despite the functional similarities, CITs and mutual funds are subject to strikingly different regulatory regimes. This reality revives an old debate about "functional regulation," a concept that posits that "similar financial products and services" should be subject to "similar regulatory schemes regardless of the historical industry classification of the institution offering the product or service."[131]

Although the different regulatory regimes for CITs and mutual funds have not been analyzed or questioned in recent years, it is important to acknowledge that there was robust engagement with this issue throughout the 1960s-80s. As the GAO reported in 1986, "there has been public debate by federal regulators, trade associations and congressional committees on whether the current federal structure for regulating financial institutions should be changed."[132] Others have referred to this period as characterized by "intense and sometimes bitter controversy between banks and the securities industry over attempts by banks to expand the scope of their collective investment activities."[133] Scholars writing about CITs in the 1970s and 1980s observed that "[a] less desirable aspect of collective investment funds, however, is the somewhat illogical and inconsistent statutory framework that governs their establishment and operation."[134]

The "functional regulation" debate of the 1960s and 1970s was left unresolved. Developments over the last four decades merit a revival of the key questions. Most importantly, both the regulatory framework for CITs and the legal regime for U.S. retirement plans predate the development of defined contribution plans, and the widespread use of CITs in such plans. That so many Americans' hard-earned retirement savings are invested in CITs—almost certainly without their appreciation—merits closer consideration of whether the existing regulatory framework for CITs is justified and whether the competition between mutual funds and CITs promotes retirement security.[135] Moreover, to the extent

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[131] U.S. GEN. ACCT. OFF., REPORT TO MEMBERS OF CONGRESS: FUNCTIONAL REGULATION: AN ANALYSIS OF TWO TYPES OF POOLED INVESTMENT FUNDS 1 (1986), https://www.gao.gov/assets/ggd-86-63.pdf [https://perma.cc/W22A-3FTR].

[132] *Id.*

[133] Wade, *supra* note 7, at 362.

[134] *Id.*

[135] In a 2022 proposed rule, the SEC acknowledged and asked for additional feedback on the possibility that the agency's proposed swing pricing requirement would "cause or incentivize investors to move their assets out of the funds that must implement swing pricing into other investment vehicles that do not use swing pricing, such as…collective investment trusts." *See* Open-End Fund Liquidity Risk Management Programs and Swing Pricing; Form N-PORT Reporting, 87 FR 77172 (proposed Dec. 16, 2022)(to be codified at 17 CFR 270-74). For a discussion of the relationship between innovation and regulation more broadly, see, e.g., Merton H. Miller, *Financial Innovation: The Last Twenty Years and the Next*, 21 J. FIN. & QUANTITATIVE. ANALYSIS 459 (1986).

that retirement savings play a critical role in U.S. capital markets, further analysis is needed to assess how the shift to CIT may impact the incentives and behavior of asset managers as institutional investors.

III. Corporate Governance & Securities Law Considerations

This Section sets forth the growing and underappreciated role of CITs in U.S. corporate and investment governance. In so doing, it develops an interdisciplinary research agenda on CITs.

A. Institutional Investor Governance

Without consideration of CITs, existing analyses present an incomplete picture of the institutional investor landscape, including institutional shareholder engagement and activism. While there is an extensive body of research on institutional investors, and particularly the so-called "Big Three," the traditional focus has been on the organization, incentives, and agency cost concerns of mutual funds.[136] More recently, however, scholars have suggested that in focusing on mutual funds, and on index funds in particular, scholars have overlooked the substantial portion of assets managed by the likes of BlackRock and State Street that are not in mutual funds.[137] CITs fall squarely in that latter category, and their behavior—both as investment intermediaries and as shareholder activists—may challenge traditional narratives on institutional investors.[138]

Unlike mutual funds, CITs are not subject to proxy voting disclosure and there is no public accountability for how bank trustees or their subadvisors cast votes.[139] As institutional investors like BlackRock, Vanguard, and State Street

[136] Dorothy Lund & Adriana Robertson, Giant Asset Managers, the Big Three, and Index Investing (Apr. 14, 2023) (unpublished manuscript), *available at* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4406204 [https://perma.cc/KVJ5-SYZT] (observing that "a robust literature describes the incentives and stewardship practices of the "Big Three" asset managers (BlackRock, Vanguard, and State Street Global Advisor").

[137] Lund & Robertson, *supra* note 136, at 13-14 (emphasizing that "index equity mutual funds represent a only a portion of assets managed by the Big Three" and noting that "while the overwhelming majority of the assets managed by Fidelity and Vanguard are in mutual funds, [mutual funds] represent less than a third of the assets managed by State Street, and less than 60% of the assets managed by BlackRock").

[138] *See, e.g.,* Hudson, *supra* note 6 (describing the shareholder proposals submitted by CITs to Disney and Apple). Recent scholarship has advocated explicitly for the use of CITs as a means of preserving "collective shareholder voice" in a defined contribution retirement system. *See* Webber, *supra* note 36 at 1019 (suggesting that CITs in the private sector could be "the same as public pension funds are now, retaining the collective shareholder voice, but not guaranteeing workers' fixed payments in retirement").

[139] CITs claim to set their own "investment objectives, guidelines, and/or policies that must be accepted as a condition for investment." In response to the DOL's 2022 Final Rule on Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights, which requires that

have accumulated ever larger stakes in U.S. public companies over the last two decades, their voting behavior has come under increasing scrutiny.[140] The attention has intensified as the range of issues subject to precatory shareholder votes has expanded to include proposals on matters such as environmental sustainability, human capital management, equity and diversity, and corporate political spending. Such scrutiny is possible only because when BlackRock, Vanguard, and State Street cast votes on behalf of mutual funds (and ultimately on behalf of the individual investors), they must publicly report their votes to the SEC. While the voting records have landed institutional investors in the crosshairs of various social and political debates, they nevertheless provide an important measure of public accountability and oversight.[141]

The same oversight and accountability are not currently required for the trillions of dollars invested through CITs.[142] Back in 2002, right after the SEC finalized new requirements for the disclosure of proxy votes by mutual funds as part of "a government attempt to restore investor confidence after a series of corporate scandals" there was some indication that the OCC was "weighing whether to require bank trust departments to disclose how they cast proxy votes on behalf of the clients whose money they manage through investment pools."[143] In fact, mutual funds had complained that the SEC rule had excluded CITs and had thus created "an unlevel playing field."[144]

But the OCC never did enact such rules for CITs, and two decades and trillions of dollars later, asset managers are able to "level the playing field"

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investment managers of pooled investment vehicles reconcile the investment policies of the participating plans and, in the case of proxy voting, "vote relevant proxies to reflect such policies in proportion to each plan's economic interest in the pooled investment vehicle," the American Bankers Association argued that such a requirement does not "reflect current industry standard practice followed by investment managers for collective investment funds." Prudence and Loyalty in Selecting Plan Investments and Exercising Shareholder Rights, 87 Fed. Reg. 73,822, 73,851 (Jan. 30, 2023) (to be codified at 29 C.F.R. pt. 2550). The Association further raised concerns that the DOL guidance on proxy voting "may be inconsistent with Office of the Comptroller of the Currency expectations regarding that bank's treatment of participants in a pooled investment fund." Letter from Am. Bankers Ass'n, to Off. of Regs. & Interpretations, Emp. Benefits Sec. Admin, U.S. Dep't of Lab. (Dec. 13, 2021), https://www.aba.com/advocacy/policy-analysis/aba-letter-to-dol-on-esg-investments-proposal [https://perma.cc/TM66-KJ53].

140 *See, e.g.*, John D. Morley, *Too Big to Be Activist*, 92 S. CAL. L. REV. 1407, 1410 (2019) (describing the "tidal wave" of academic scholarship); Lucian Bebchuk, Alma Cohen & Scott Hirst, *The Agency Problems of Institutional Investors*, 31 J. ECON. PERSPS.. 89, 90 (2017);

141 *See, e.g.*, Jill E. Fisch & Jeff Schwartz, *Corporate Democracy and the Intermediary Voting Dilemma*, 102 TEX. L. REV. 1 (2023).

142 Some CITs hold equities directly in the trusts. Others may invest some of the trust assets in mutual funds, but the proportion of CIT assets in mutual fund vehicles is not reported, nor it is possible to calculate from publicly available data.

143 Kathleen Day, *Trusts May Be Next to Get Proxy Rules*, WASH. POST (Jan. 31, 2003), https://www.washingtonpost.com/archive/business/2003/01/31/trusts-may-be-next-to-get-proxy-rules/a5727e48-ec75-44a2-82b0-7fe7635af0c5/ [https://perma.cc/KL66-77JJ].

144 *Id*.

themselves by setting up CITs and encouraging retirement plans to move their assets out of mutual funds and into CITs. To the extent that the same considerations that prompted proxy vote disclosure requirements in the first place are still important, the disclosure requirements for CITs should be reevaluated. Such a reevaluation should take into account the reality that bank stability—and not investor confidence in capital markets—is the primary concern of the OCC.

B. Investment Fund Governance

Applying the "Investment Fund Theory to CITs: Scholars have focused extensively on the governance of different types of investment funds, and particularly mutual funds. A dominant theory in the field suggests that "investment funds (i.e., mutual funds, hedge funds, private equity funds, and their cousins) are distinguished not by the assets they hold, but by their unique organizational structures, which separate investment assets and management assets into different entities with different owners.[145] In this structure, "the investments belong to 'funds,' while the management assets belong to 'management companies.'" Scholars have argued that this structure ultimately benefits investors. Although the separation of funds and managers restricts the investors' rights to control their managers and to share in their managers' profits and liabilities, typical investment fund features make these restrictions efficient. In particular, "powerful investor exit rights substitute for control rights."[146] Under this theorical framework, the voting rights given to mutual fund shareholders are not valuable to the shareholders and will not be used.

To the extent that CITs are "functionally" similar to mutual funds (and might be considered to be a kind of investment company but for the statutory exemptions) but are organized and governed differently, they offer an important test case for the application of the "separation of funds and managers" theory.[147] Indeed, in some sense, CITs defy the "separation of funds and managers" framework because the trusts are maintained by the banks and the banks serve as the trustees.[148] Moreover, in the CIT structure, investors have no voting rights whatsoever and, at the same time, have limited exit rights.[149] The only possible

[145] Morley, *supra* note 129.

[146] *Id*.

[147] In the 1960s, the SEC and the OCC leadership engaged in a debate about the proper characterization of CITs. William L. Cary, who served chairman of the SEC between 1961-64, proposed viewing the CIT or the fund itself as separate from the bank, and subject to SEC regulation as an "ectoplasmic investment company." The Comptroller of the Currency disagreed and maintained that "[t]he fund is the bank—it is the board of directors that is responsible for its operation. There is not such distinction we see whereby the fund becomes a separate creature." *See* Webb, *supra* note 36 at 341–43.

[148] Although the trusts are maintained by the banks, trust assets are not available to the creditors of the bank.

[149] For a discussion of "lock in" in the mutual fund context, *see* Anne M. Tucker, *Locked In: The Competitive Disadvantage of Citizen Shareholders*, 125 YALE L.J. F. 163 (2015),

substitute for voice and exit in the CIT context is the intermediation by plan sponsors (i.e., employers) in the initial negotiation of the CIT terms, and in the ongoing monitoring of CITs required by ERISA. However, as described below, employers may not be well suited for this role.

Addressing Systemic Risks from Regulatory Gaps: CITs and mutual funds are subject to different liquidity, pricing, reporting, and redemption rules. The SEC has begun to raise concerns about the risks stemming from such regulatory gaps and the "financial fires" that could spread in the absence of consistent regulation.[150] Reform would require serious agency coordination (among agencies with different mandates and missions) as well as agreement on the desired policy goals. History suggests that such agreement and coordination may be difficult to achieve without Congressional involvement.

IV. RETIREMENT SECURITY & CITS

This Section describes the implications stemming from the embrace of CITs in employer-sponsored retirement plans.

Lower fees and flexibility are important, but the savings must be weighed against the additional risks associated with CITs. There is no question that all else equal, retirement savers are better off when they pay smaller investment management and administrative fees. Although the fee data for CITs is not publicly available and one cannot simply compare the fee structures for different CITs across retirement plans, industry reporting suggests that CITs do offer lower fees for "similar" investment products. [151] But, for the reasons described below, CITs come with certain costs—particularly decreased transparency and less substantive regulation—that have to be considered, both at the individual plan level, and at a macro level for all U.S. retirement savers.

The regulatory framework is based on an outdated premise. Defined contribution plans alter the regulatory calculus and cast doubt on the merits of relying on banking regulation to protect individual participants. As the SEC

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http://www.yalelawjournal.org/forum/locked-in-the-competitive-disadvantage-of-citizen-shareholders.

[150] Gensler, *supra* note 4.

[151] *See, e.g.*, DESAI & DAUWEN, *supra* note 7, at 18 (suggesting that their "panel of experts was generally confident that the relative cost savings of CITs over mutual funds stood in the 10 to 30 basis point range" and noting that CITs also provide greater flexibility in the types of investments and investment strategies). In recent years, some "excessive fee" retirement plan litigation has included the argument that plan administrators breached their fiduciary duties by failing to consider CITs as a cheaper alternative to mutual funds. *See, e.g.*, Parker v. Tenneco Inc., No. 23-10816, slip op. at X (E.D. Mich. Aug. 21, 2023) (alleging that that "[d]efendants failed to offer the Plan's participants similar investment options to those in the Plan that were less costly and equally or better-performing, failed to take advantage of savings offered by lower cost share classes of mutual funds already in the Plan, and failed to consider investment vehicles with lower fees than those in the Plan, such as collective trusts (also called 'collective investment trusts' and 'collective trust funds'").

noted three decades ago, "[w]hen the securities laws exceptions for pooled investment vehicles were enacted, pension plans were predominantly 'defined benefit plans' offered by large and generally sophisticated employers."[152] That is, when the decision to allow CITs to operate outside the securities law requirements was made, the potential "harms" of investing in CITs were borne by employers who, in the context of defined benefit plans, were ultimately responsible for paying the promised pension benefits to employees, irrespective of how the underlying investments performed. Today, a wide swath of the general public is exposed to CITs and directly affected by their performance. While employers still serve as the intermediaries between CIT sponsors and individual employee participants, the risk is borne by individual participants.

The current regulatory structure puts a lot of responsibility on, and trust in, employer intermediaries. Employers may not be up to the task, and ERISA's "fiduciary standards" may not be the right regulatory tool. Employee benefits scholars have identified the challenge of "fiduciary governance" under ERISA. They have emphasized that the development and drafting of ERISA predate the rise of 401(k) plans. In the 1960s and 1970s, defined benefit pension plans were the norm. To address certain shortcomings in defined benefit plans, ERISA, which was enacted in 1974, imposed extensive vesting, funding, and insurance requirements to govern employer conduct in the administration of defined benefit pension plans. ERISA's fiduciary provisions were "stapled on" at the end as just one piece of ERISA's protective regime.[153] However, with the shift to defined contribution plans, many of ERISA's substantive rules no longer apply, and the trust-based fiduciary regime has taken on an increasingly prominent role in regulating the provision of retirement benefits.[154] One challenge with this "fiduciary governance" approach, particularly with respect to employers, is that employers generally do not conceive of themselves as fiduciaries of their employees, may not be aware of the ERISA fiduciary requirements, and, in some cases (and particularly in the case of smaller employers), may not have the resources or expertise to provide effective intermediation between CITs and individual participants. Moreover, the fiduciary *standard* has the benefit of

[152] U.S. SEC. & EXCH. COMM'N, *supra* note 73, at 119.

[153] Frank Cummings, *Panel Discussion, ERISA and the Fiduciary, Symposium, ERISA at 40: What Were They Thinking?*, 6 DREXEL L. REV. 359, 376 (2014) (stating that the fiduciary provisions were effectively stapled on after the drafting of the substantive rules).

[154] Shnitser, *supra* note 86; *see also* Dana M. Muir, *An Agency Costs Theory of Employee Benefit Plan Law*, 43 BERKELEY J. EMP. & LAB. L. 361 (2022) (discussing the disconnects between the structure of donative trusts and employee benefit plans); Peter J. Wiedenbeck*, Untrustworthy: ERISA's Eroded Fiduciary Law,* 59 WM. & MARY L. REV. 1007 (2018) (describing the "taming" or ERISA fiduciary law).

flexibility but does not provide concrete guidance for employers in their interactions with financial institutions.[155]

Because CITs are subject to fewer disclosure and reporting requirements, it is harder to compare CITs across plans. The lack of data limits oversight and enforcement. Whereas price and performance data for mutual funds is readily available to the public, comparable data for CITs is not. Existing requirements focus on the provision of information to plan sponsors but not to the public,[156] and regulatory efforts to expand CIT disclosure requirements have faced significant opposition.[157] While some financial institutions (such as Morningstar) may collect relevant data, they do not make the data publicly available. Notably, Morningstar itself has acknowledged the relative lack of transparency in CITs[158] as compared to mutual funds, and other proponents of CITs have likewise recognized the need to improve transparency, particularly with respect to the

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[155] *See, e.g.*, Natalya Shnitser, *Fiduciary Governance for 401(k)s*, REGUL. REV. (Apr. 27, 2023), https://www.theregreview.org/2023/04/27/shnitser-fiduciary-governance-for-401ks/ [https://perma.cc/L9V7-WJSZ]; Brendan S. Maher, *Regulating Employment-Based Anything*, 100 MINN. L. REV. 1257 (2016).

[156] As T.Rowe Price notes in its literature on CITs, "CITs do not trade on an exchange, and they may be less transparent than mutual funds since daily prices aren't publicly available. Investment information and historical return data can be limited to an individual (or specific) trust's inception. Like any new investment option, performance evaluations may be limited due to the lack of long-term data. However, CIT providers are required to furnish data to plan fiduciaries and may also provide fact sheets or data from third parties that can facilitate research." T. Rowe Price, https://www.troweprice.com/content/dam/fai/Investments/CIT/literature/cit-brochure.pdf

[157] Recent DOL efforts to amend reporting requirements for CITs – such as in the proposed SECURE Act and Related Revisions to the Form 5500 – have faced industry pushback. Annual Reporting and Disclosure, 86 Fed. Reg. 51,284 (Sept. 2, 2021) (to be codified at 29 C.F.R. pt. 2520). The Coalition of Collective Investment Trusts argued that the proposal to require certain Collective Trusts (CCTs) that are "invested primarily in hard-to-value assets to, themselves, be identified as hard-to-value assets" would "fail[] to take into account the significant evolution of CCTs over the past 15 years," including the improved disclosure requirements over that period. The Coalition also emphasized that "CCTs are regulated by state banking regulators and are subject to a robust examination cycle," that "trustees or sponsors of CCTs generally are ERISA fiduciaries to the plan assets invested in their vehicles and manage them in accordance with an ERISA fiduciary standard" and that therefore, "singling out CCTs in the manner proposed is unwarranted and does not serve any underlying policy rationale." Letter from Clifford Kirsch & Carol McClarnon, Coal. of Collective Inv. Trs., to Off. of Reguls. & Interpretations, Emp. Benefits Sec. Admin., U.S. Dep't of Lab. (Nov. 1, 2021), https://www.dol.gov/sites/dolgov/files/EBSA/laws-and-regulations/rules-and-regulations/public-comments/1210-AB97/00109.pdf [https://perma.cc/7MLK-6LES].

[158] In advocating for 403(b) plan access to CITs, Morningstar acknowledged the "limited data availability" of CITs. *See* SETHI ET AL., *supra* note 34. Furthermore, in its reporting on CIT trends, Morningstar noted that its calculations are limited by the inconsistent reporting of fees by CITs. *See* MITCHELL, *supra* note 5 ("Our CIT data is collected from CIT providers and covers more than 7,500 tiers of CITs. Some of the tiers reported to our database are "gross of fee" share classes, meaning they do not report net-of-fee performance, as the fee is negotiable and/or the tier is only available to a restricted group of investors. When we compare CIT and mutual fund costs, we exclude these share classes so as not to distort the data.").

disclosure of "all-in" costs.[159] In the absence of robust, publicly available information, the ability of analysts, scholars, and private plaintiffs to provide oversight and enforcement is necessarily limited.

Existing litigation concerning CITs has shown that some asset managers and other service providers may be incentivized to push retirement plan participants into newly formed, affiliated CITs. In recent years, several cases brought by plans participants have accused plan service providers of pushing plan assets into CITs newly established by affiliated entities.[160] Such cases raise the possibility of conflicts of interest that can arise when asset managers are rushing to enter the CIT market.[161]

Lack of substantive limits on underlying investments, together with the risks from "herding" and "network interconnectedness" present risks to U.S.

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[159] Jackson, *supra* note 36, at 132-151 (observing that "legal protections at the collective investment trust level are not fully comparable to mutual fund regulation," noting that "[e]ven proponents of CITs recognize the need to improve product transparency, including more comprehensive disclosure of all in-costs," and citing survey results "that less than a quarter of CIT providers publicly report 'all-in' costs"); *see also* Lee Barney, *Education and Transparency Two Issues for CIT Use in DC Plans*, PLANSPONSOR (Aug. 22, 2019), https://www.plansponsor.com/education-transparency-two-issues-cit-use-dc-plans/ (reporting that "their lack of transparency" is a challenge for CITs that threatens their adoption and noting employers' concern about consistent, public reporting).

[160] Since 2009, there have been nearly 200 ERISA cases referencing collective investment trusts, a statistic that reflects generally the growing popularity of CITs in retirement plan investment menus.

[161] For example, in a recent case, plaintiffs alleged that "instead of acting in the exclusive best interest of participants, Aon Hewitt [Investment Consulting, Inc. ("Aon Hewitt"), which served as the plan's discretionary investment manager] acted in its own interest by causing the Plan to invest in Aon Hewitt's proprietary collective investment trusts, which benefitted Aon Hewitt at the expense of Plan participants' retirement savings.". Complaint-Class Action at 2, Miller v. Astellas US LLC, No. 20CV03882 (N.D. Ill. July 1, 2020). Also notable in that case was a description of the CIT organization and fee structure:

> As a non-depository bank, Aon Trust Company LLC maintains the Aon Hewitt collective investment trusts and is the trustee of the funds. Both Aon Trust Company and Aon Hewitt are wholly owned subsidiaries of Aon Consulting, Inc. Aon Trust Company hired [Aon Hewitt Investment Consulting, Inc. ("Aon Hewitt")]—effectively hired itself—as the investment adviser to perform investment advisory and investment management services with respect to each fund. . . . Aon Hewitt does not actually manage the assets of the Aon Hewitt collective investment trusts. Aon Hewitt hires one or more unaffiliated investment managers (or sub-advisors) to do the actual investing. Aon Hewitt collects an investment "advisory" fee charged to fund investors for its services in hiring the manager or sub-advisor, and Aon Trust Company charges an additional trustee fee. This structure results in investors paying multiple layers of fees, including an investment "advisory" fee to Aon Hewitt even though Aon Hewitt is not doing the actual selection of securities.

Id. at 18–19. In June 2023, the parties agreed to settle for $9.5 million and certain plan governance changes. *See* Robert Steyer, *Astellas, Aon Settle 401(k) Lawsuit for $9.5 Million*, PENSIONS & INVS. (June 26, 2023), https://www.pionline.com/courts/astellas-aon-settle-401k-lawsuit-95-million [perma]. Another case involving Aon CITs settled in February of 2024 for $7.5 million. *See* Jacklyn Wille, *Aon, Centerra Sign $7.5 Million Settlement in 401(k) Class Suit*, BLOOMBERG L. (Feb. 5, 2024, 9:54 AM), https://news.bloomberglaw.com/employee-benefits/aon-centerra-sign-7-5-million-settlement-in-401k-class-suit [https://perma.cc/8EP3-MB3F].

retirement savers. As noted recently by SEC Chair Gensler, the different liquidity and pricing rules for mutual funds and CITs raise concerns about "financial fires can spread from regulatory gaps."[162] Such risks are unlikely to be addressed solely through the imposition of fiduciary standards on plan sponsors and bank trustees.

V. CONCLUSION

In May 2023, the head of Vanguard Group's institutional investor group praised the House Financial Services Committee after it passed a bill that would expand access to CITs. The statement of support argued that as a matter of parity, "educators, and other employees of non-profits and schools, should have access to the same low-cost investment vehicles, such as collective investment trusts, as their counterparts in other retirement plans."[163] Notwithstanding the industry and Committee support for the bill, the Congressional record reveals limited recent discussion of collective investment trusts and no consideration of potential downsides to CITs. As this Article has shown, such downsides do exist and they must be considered carefully alongside the benefits to ensure that the embrace—and potential expansion of—CITs in U.S. retirement plans promotes, rather than endangers, retirement security. Furthermore, closer agency coordination and analysis is necessary to evaluate the impact of unreported proxy votes on U.S. corporate governance, and the impact of differing liquidity and valuation rules on the stability of U.S. financial markets. Nearly a century ago, the banks' foray into retail investment products contributed to the 1929 crash. Although much has changed since then, the lessons from the past should inform proactive regulatory responses to promote the soundness of the financial system, preserve the integrity of the U.S. capital markets, and provide retirement security for U.S. workers.

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[162] Gensler, *supra* note 4. A 2013 report by the Office of Financial Research identifies redemption risk in collective investment vehicles as one of "the key factors that make the [asset management industry] industry vulnerable to shocks." OFF. OF FIN. RSCH., ASSET MANAGEMENT AND FINANCIAL STABILITY (2013), https://www.financialresearch.gov/reports/files/ofr_asset_management_and_financial_stability.pdf [https://perma.cc/9QZ8-DJ9V].

[163] Croce, *supra* note 35.

APPENDIX

Table 1: CIT Investment Strategies as of 2023[164]

	Estimated Net Flow ($Mil), 1-Yr	**Market Share Basis: Total Net Assets ($Bil), as of 09-2023**	**Market Share%**
Allocation	175,328	1,652.96	34.906
US Equity	168,179	1,515.71	32.008
International Equity	22,193	792.72	16.740
Taxable Bond	32,670	690.03	14.572
Money Market	(2,737)	61.42	1.297
Sector Equity	(203)	19.25	0.406
Commodities	8	2.54	0.054
Alternative	(193)	0.53	0.011
Nontraditional Equity	165	0.21	0.004
Municipal Bond	(2)	0.04	0.001
Total	**395,408**	**4,735**	**100.00**

[164] Information in this table is from the Morningstar Direct database.