

MEMO# 2962

July 30, 1991

SEC STAFF NO-ACTION POSITION PERMITS UITs TO REQUIRE TRUSTEES TO SUBSTITUTE NEW BONDS FOR REFUNDED BONDS

July 30, 1991 TO: UNIT INVESTMENT TRUST MEMBERS NO. 27-91 RE: SEC STAFF NO-ACTION POSITION PERMITS UITs TO REQUIRE TRUSTEES TO SUBSTITUTE NEW BONDS FOR REFUNDED BONDS _____ In a recently released no-action letter issued to two co- sponsors of unit investment trusts, the staff of the Division of Investment Management stated that it would not recommend that the Commission take enforcement action with respect to any unit investment trust created by the co-sponsors in the future solely because the trust indenture requires the trustee to accept bonds issued pursuant to a plan of refunding or refinancing in exchange for or substitution of a bond then held in the trust's portfolio. Copies of the no-action request and the staff's response are attached. In their no-action request, the co-sponsors explained that many of the municipal bonds held by their unit investment trusts have optional refunding or refinancing provisions pursuant to which the issuer has the right to call the bonds prior to their stated maturity and to issue new bonds to finance the redemption. Although issuers typically utilize the call feature to take advantage of lower interest rates, resulting in a lower coupon interest rate on the new bonds, according to the co-sponsors this effect would be offset at least in part by a premium normally payable to bond holders on the call date. In addition, the co- sponsors argued, this proposal would benefit unitholders, who would be assured of a continuous income stream and could avoid the transaction costs that would be involved in connection with reinvesting a distribution of principal received if the bonds were called and not replaced. The staff's favorable response relied in particular on the sponsors' representations regarding: (1) the role of the independent evaluator; (2) disclosures to be made on a trust's prospectus cover and by sales representatives to potential clients regarding the substitution feature; (3) the fact that the issuer of the refunded bonds and the substituted bonds would be the same and the bonds would be substantially identical; (4) certain provisions that would be inserted into the trust indenture including in particular a provision requiring that any substituted bonds be issued pursuant to a firm commitment underwriting; (5) the fact that the substituted bonds would not generate any increase in fees payable to the independent evaluator or the trustee; and (6) the fact that neither the sponsors nor any affiliated person thereof would receive any fee in connection with the purchase of the substituted bonds. Frances M. Stadler Assistant General Counsel

Attachments

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