

MEMO# 4127

September 24, 1992

INSTITUTE PROPOSES CHANGES TO MARGIN TREATMENT OF INVESTMENT COMPANY SHARES

September 24, 1992 TO: UNIT INVESTMENT TRUST COMMITTEE NO. 54-92 SEC RULES COMMITTEE NO. 72-92 CLOSED-END FUND COMMITTEE NO. 21-92 RE: INSTITUTE PROPOSES CHANGES TO MARGIN TREATMENT OF INVESTMENT COMPANY SHARES

The Institute has submitted a rulemaking petition to the Federal Reserve Board proposing that the Board amend Regulation T to eliminate certain inequities that currently exist in the treatment of extensions of credit by brokers or dealers with respect to securities issued by investment companies. Such securities are treated as "margin equity securities" under Regulation T, which means that a broker or dealer may extend credit to a customer holding those securities equal to 50 percent of the value of the securities or the percentage set by the regulatory authority where the trade occurs, whichever is greater. In contrast, in the case of "exempted securities" (as defined in the Securities Exchange Act of 1934), a broker or dealer may extend credit in an amount equal to the "good faith" loan value of the securities (which is likely to be more than 50 percent). Thus, under Regulation T, an investor who owns exempted securities may borrow the good faith loan value of those securities from a broker or dealer, but an investor who owns a proportionate interest in a pool of those same securities through ownership of shares of an investment company, can borrow only 50 percent of the market value of those shares. Moreover, under Regulations U and G (governing extensions of credit by banks and other lenders), the maximum loan value of investment company securities is their good faith loan value, provided that the investment company has at least 95% of its assets continuously invested in exempted securities. Thus, brokers and dealers extending credit to customers with respect to investment company securities are at a competitive disadvantage compared to banks and other persons in terms of the amount of credit they can extend. The Institute's proposal would eliminate the above discrepancies by amending Regulation T to provide that brokers and dealers may extend to customers holding investment company securities in a margin account the good faith loan value of those securities, provided that the investment company has at least 95% of its assets continuously invested in exempted securities. Copies of the rulemaking petition and supporting memorandum that the Institute filed with the Federal Reserve Board are attached. We will keep you informed of developments. Frances M. Stadler Assistant Counsel

Attachments

Copyright © by the Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice.