

MEMO# 7069

June 29, 1995

PROPOSED AMENDMENTS TO REGULATION T TO LIBERALIZE MARGIN TREATMENT OF SECURITIES ISSUED BY INVESTMENT COMPANIES

1 See Memorandum to Unit Investment Trust Committee No. 54-92, SEC Rules Committee No. 72-92 and Closed-End Fund Committee No. 21-92, dated September 24, 1992. June 29, 1995 TO: CLOSED-END FUND COMMITTEE No. 31-95 SEC RULES COMMITTEE No. 78-95 UNIT INVESTMENT TRUST COMMITTEE No. 52-95 RE: PROPOSED AMENDMENTS TO REGULATION T TO LIBERALIZE MARGIN TREATMENT OF SECURITIES ISSUED BY INVESTMENT COMPANIES

The Institute is pleased to report that the Federal Reserve Board recently issued a release seeking comments on a series of proposed amendments to Regulation T, including amendments based on an Institute proposal that would liberalize the margin treatment of securities issued by registered investment companies.¹ A copy of the proposing release is attached. The proposed changes concerning margin treatment of investment company securities are discussed on page 10 and set forth on pages 26-27 (definitions) and 50 of the attached release. Regulation T governs extensions of credit by brokers and dealers. In its current form, Regulation T treats securities issued by investment companies as "margin equity securities," meaning that a broker or dealer may extend credit to a customer holding these 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 as currently in effect, an investor who owns exempted securities may borrow the good faith loan value of those securities from a broker or dealer, while 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. As the Institute had recommended in a submission to the Federal Reserve Board in 1992, the Board has proposed amendments to Regulation T to eliminate this discrepancy. Specifically, the proposed amendments would allow brokers and dealers to give "good faith" loan value to securities issued by an "exempted securities mutual fund," which would be defined as "any security issued by an investment company registered under section 8 of the Investment Company Act of 1940 . . . , provided the company has at least 95 percent of its assets continuously invested in exempted securities (as defined in section 3(a)(12) of the [Securities Exchange] Act." This proposed change also would conform the margin treatment of investment company securities under Regulation T with that under Regulations G and U

(governing extensions of credit by banks and other lenders). Under the Board's proposal, money market mutual funds also would be eligible for good faith loan value treatment under Regulation T. Another amendment proposed by the Board would define money market mutual funds as "cash equivalents." As a result, such securities could be used to cover a put option written in a customer's cash account. Comments on the proposed amendments must be filed by August 28th. If there are issues you would like the Institute to consider addressing in its comment letter, please contact the undersigned at (202) 326-5822 by Tuesday, August 1st. Frances M. Stadler Associate Counsel Attachment

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