

MEMO# 5935

May 31, 1994

SEC PROPOSED RULE TO PERMIT FUTURES COMMISSION MERCHANTS TO HOLD INVESTMENT COMPANY FUTURES MARGIN

May 31, 1994 TO: ACCOUNTING/TREASURERS COMMITTEE NO. 27-94 SEC RULES
COMMITTEE NO. 59-94 RE: SEC PROPOSED RULE TO PERMIT FUTURES COMMISSION
MERCHANTS TO HOLD INVESTMENT COMPANY FUTURES MARGIN

The Securities and Exchange Commission has proposed Rule 17f-6 under the Investment Company Act of 1940, to permit futures commission merchants ("FCMs") and commodity clearing organizations to hold custody of margin in connection with certain futures and options transactions by investment companies. A copy of the Commission's proposing release is attached. Section 17(f) of the Investment Company Act generally requires that investment companies maintain their assets only in the custody of a bank, a member of a national securities exchange or a national securities depository. FCMs and commodity clearing organizations do not fit within any of these authorized categories. As a result, currently, an investment company that engages in futures and options transactions typically deposits initial margin in a special account in the name of the FCM at its custodian bank. Proposed Rule 17f-6 would eliminate the need for such "third party" custody arrangements (although they would still be permitted) by allowing a registered management investment company to place and maintain assets with an FCM in amounts necessary to effect exchange-traded futures contracts and commodity options, provided certain conditions were met. For example, among other things, the proposed rule would specify minimum net capital requirements for FCMs holding investment company assets, would require a written contract between an investment company and an FCM that would contain certain required provisions and would require the investment company's board of directors to select FCMs and monitor the arrangements (although the board could delegate these responsibilities to the investment adviser or fund officers, subject to general oversight and procedural requirements). Comments on the proposed rule must be filed within 60 days of its publication in the Federal Register. If there are issues you would like the Institute to consider including in its comment letter, please contact me at (202) 326-5822 by Tuesday, June 21st. Frances M. Stadler Associate Counsel Attachment

should not be considered a substitute for, legal advice.