The Asset Management Industry
SERVING INDIVIDUAL INVESTORS
INVESTMENT COMPANY INSTITUTE

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ICI Joins Letter to SEC Addressing Whether Certain Syndicated Loans are Securities

[35347]

June 13, 2023

TO: ICI Members SUBJECTS: Compliance
Investment Advisers
Litigation & Enforcement
Portfolio Oversight
Risk Oversight RE: ICI Joins Letter to SEC Addressing Whether Certain Syndicated Loans are Securities

Earlier this month, ICI joined several other trade associations in a letter to the SEC addressing whether certain syndicated loans are securities. In Kirschner v. JP Morgan Chase Bank, N.A. et al. (2d Cir., No. 21-2726), the Second Circuit Court of Appeals is considering that question.[1] After oral argument, the court issued an order "solicit[ing] any views that the United States Securities and Exchange Commission may wish to share" regarding "whether the syndicated term loan notes at issue in this appeal are securities under Reves."[2]

In May, the Loan Syndications and Trading Association (LSTA) submitted to the SEC a letter explaining the adverse consequences that would arise for market participants if the SEC were to call into question the decades-long understanding that syndicated loans are not securities. LSTA's letter urges the SEC to submit a brief that reaffirms the market understanding that syndicated term loans are not securities. LSTA's letter argues that a statement from the SEC that syndicated loans are securities would lead to potential market disruption and inefficiencies. Moreover, it would represent a drastic departure from the SEC's historical stance, lead to regulatory uncertainty, and harm existing reliance interests. It concludes by stating that if the SEC seeks to change the historical treatment of syndicated loans, it should undertake a measured, public process.

Linked below, the letter from ICI and several other trade associations (which includes LSTA's SEC submission and its amicus brief to the Second Circuit Court) expresses support for the points presented in the LSTA's letter, urges the SEC to confirm that syndicated loans are not securities,[3] and underscores certain considerations that may bear on the SEC's response. ICI's primary concern is that a regulatory change in status of these loans would

create immediate uncertainty and disruption. This in turn could lead to interruptions or impediments to secondary market trading, harming mutual funds that invest in these loans.

Matthew Thornton
Associate General Counsel

Notes

[1] In April 2014, institutional investors purchased debt obligations of Millennium Laboratories LLC from a group of lenders. After Millennium filed for bankruptcy, Marc Kirschner, as trustee of the Millennium Lender Claim Trust, sued the lenders in the U.S. District Court for the Southern District of New York, claiming, among other things, that the debt obligations constituted securities, and thus were subject to stringent disclosure rules under state securities laws. The lender defendants moved to dismiss the securities law claims on the grounds that a syndicated bank loan is not a security, and a loan syndication is not a securities distribution. In May 2020, the U.S. District Court held that the debt obligations did not constitute securities and granted the defendants' motion to dismiss all such claims. The trustee then filed an appeal to the Second Circuit to have the decision overturned.

[2] In Reves v. Ernst & Young, 494 U.S. 56 (1990), the Supreme Court set out four factors relevant to whether a particular instrument is a "security" under the Securities Act of 1933 and the Securities Exchange Act of 1934: (1) "the motivations that would prompt a reasonable seller and buyer to enter into" the transaction—that is, whether the transaction has a "commercial" or "investment" purpose; (2) "the 'plan of distribution' of the instrument"—that is, "whether it is an instrument in which there is 'common trading for speculation or investments'"; (3) "the reasonable expectations of the investing public"; and (4) whether "the existence of another regulatory scheme" makes "application of the Securities Acts unnecessary."

[3] This joint letter—and support for the LSTA's May 2023 letter to the SEC—relates only to whether syndicated loans are "securities" under the Securities Act of 1933 and the Securities Exchange Act of 1934, and it does not question prior statements from the SEC or staff on the status of these or similar investments under the Investment Company Act of 1940.