

Opinion No. 63-51

May 7, 1963

BY: OPINION of EARL E. HARTLEY, Attorney General

TO: Mr. Howard M. Rosenthal, Counsel State Banking Department State Capitol Santa Fe, New Mexico

QUESTION

FACTS

Investment fund companies, in addition to sales of investment fund shares under a variety of plans, have available for sale to the public "periodic payment plans" in which the subscriber, on a voluntary basis, makes periodic payments in amounts which have no relationship to market values. The subscriber simply receives receipts indicating a participation in the fund shares held by a custodian. No investment fund shares are issued to the purchaser.

QUESTION

- (1) Are such periodic payment plans required to comply with Section 48-18-25 (7) insofar as the underlying securities value is measured therein?
- (2) If not, may the Commissioner of Securities, pursuant to Section 48-18-18 (F), issue rules and regulations in which standards are set up for such periodic payment plans?

CONCLUSIONS

- (1) No.
- (2) Yes.

OPINION

{*106} You ask whether periodic payment plans, described briefly above, must comply with Section 48-18-25 (7), N.M.S.A., 1953 Compilation (P.S.), which provides as follows:

"No investment funds shares shall be registered for offering and sale in this state unless the formula for determining the offering and sale price is such that at the time of sale to the public the market value, as hereinafter defined, of unpledged underlying securities and other assets of the issuer, after deduction of all accrued liabilities and established reserve accounts, is not less than 90% of such offering and sale price. Market value, for the purpose of this section 10, shall mean that value, at the hour of determination, and

as determined from time to time and from day to day as prescribed by the plan of operation set forth by the application statement, and in accordance with a prescribed method of computation, consistently applied, deemed by the trustees or directors of the issuer, and by the securities commissioner, to most accurately approach or represent realizable values at such hour of value determination."

The answer to your question depends upon the interpretation placed on Section 48-18-25 (1), N.M.S.A., 1953 Compilation (P. S.), which defines investment fund shares as follows:

"Securities of organizations known as 'Investment Funds' or 'Investment Companies' or 'Investment Trusts' shall for the purposes of this act, be designated and defined as 'Investment Fund Shares' and shall mean and include any form or certificate or other instrument representing beneficial interests in a trust or fund or shares of capital stock of a corporation, the assets of which trust or corporation consist principally of securities, and which assets are held under an appropriate agreement establishing and maintaining a trusteeship or a custodianship, for the benefit of holders of such interests or shares, by a bank or trust company having an aggregate capital, surplus and undivided profits of not less than \$ 1,000,000.00."

At first glance it might appear that under this definition periodic payment plans would have to meet the requirements of Section 48-18-25 (7), supra. However a close analysis of such periodic payment plans establishes that this is not the case.

Under the periodic payment plan the investor makes a monthly payment. The proceeds of these payments, after deduction of sales and maintenance charges, are invested in mutual fund companies. Since the planholder can discontinue these payments at any time, the company operating the periodic payment plan protects itself on the initial expense of the sale by a "front-end" sales charge whereby fifty percent of the installment payments for the first year are deducted for sales charges. All of the mutual fund shares which are purchased with the monthly payments by planholders are deposited with a bank as custodian. The bank holds such shares as trustee for the planholders.

{*107} The definition of investment shares contained in Section 48-18-25 (1), N.M.S.A., 1953 Compilation (P.S.) can reasonably refer only to the underlying **portfolio** of the mutual fund company. For example, the assets of Financial Industrial Fund, Inc., consists of portfolio securities which are deposited with the Bankers Trust Company in New York for the benefit of the Fund's shareholders. The custodianship of the trustee under the periodic payment plan covers only mutual fund shares purchased by and held for the accounts of the planholders - an entirely separate and distinct custodianship from the portfolio custodianship and one not contemplated by Section 48-18-25 (1), supra.

Sales of periodic payment plans for the acquisition of common shares of a mutual fund company involve the sale of two separate securities: (1) the common shares of the

mutual fund issued by the mutual fund company, and (2) periodic payment plan certificates. For this reason the Securities and Exchange Commission requires a separate prospectus for the periodic payment plan since this is deemed to be a separate and distinct security from the shares of the mutual fund itself.

Securities classified as periodic payment plans are never referred to in the trade as "shares", and we conclude that Section 48-18-25, regulating the sale of "investment fund shares", does not apply to the sale of periodic payment plan securities.

You also ask whether the Commissioner of Securities can issue rules and regulations in which standards are set up governing periodic payment plans. Our answer is in the affirmative.

In its definition of "securities" Section 48-18-17, N.M.S.A., 1953 Compilation (P.S.) includes "certificate of participation." Consequently, the Commissioner of Securities does have the authority to issue rules and regulation governing periodic payment plans.

By: Oliver E. Payne

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