## **SECURITIES AND EXCHANGE** COMMISSION

#### 17 CFR Parts 230, 239, and 270

[Release Nos. 33-7243; IC-21538; File No. S7-32-951

RIN 3235-AG63

## Calculation of Yield by Certain Unit **Investment Trusts**

**AGENCY:** Securities and Exchange Commission.

**ACTION:** Proposed amendments to rules and forms.

**SUMMARY:** The Commission is proposing for public comment rule and form amendments that would require certain unit investment trusts ("UITs" or "trusts") to use a uniform formula to calculate yields quoted in their prospectuses, advertisements, and sales literature. Use of the uniform formula by UITs is designed to permit investors to assess more accurately the anticipated yield from a UIT and to make comparisons of yields among UITs.

**DATES:** Comments on the proposed amendments should be received on or before January 29, 1996.

ADDRESSES: Three copies of all comments should be submitted to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street NW., Washington, D.C. 20549. All comment letters should refer to File No. S7-32-95. All comments received will be available for public inspection and copying in the Commission's Public Reference Room, 450 Fifth Street NW., Washington D.C. 20549.

# FOR FURTHER INFORMATION CONTACT:

Anthony R. Bosch, Senior Attorney, or Joseph E. Price, Deputy Chief, (202) 942-0721, Office of Disclosure and Investment Adviser Regulation, Division of Investment Management, Securities and Exchange Commission, 450 Fifth Street NW., Washington, D.C. 20549.

SUPPLEMENTARY INFORMATION: The Securities and Exchange Commission ("Commission") today is proposing for

- (1) Amendments to Form S-6 [17 CFR 239.16] under the Securities Act of 1933 [15 U.S.C. 77a et seq.] (the "1933 Act"), the form used by UITs to register securities under the 1933 Act, that would standardize the computation of yield by certain UITs in their prospectuses;
- (2) Amendments to rule 482 [17 CFR 230.482] under the 1933 Act, together with the amendments to Form S-6, that would require certain UITs including quotations of return in their

advertisements also to include a quotation of yield calculated in accordance with the formula in Form S-6; and

(3) Amendments to rule 34b-1 [17 CFR 270.34b-1] under the Investment Company Act of 1940 [15 U.S.C. 80a-1 et seq.] ("1940 Act") that would require certain UITs including quotations of return in their sales literature also to include a quotation of yield calculated in accordance with the formula in Form

#### **Executive Summary**

The Commission is proposing to adopt a uniform formula, called the "Estimated Yield Formula," for the calculation of the anticipated yield of UITs that invest substantially all of their assets in fixed income securities ("Fixed Income UITs"). Under the proposed rule and form amendments, a Fixed Income UIT would be required to include in its prospectus a yield quotation calculated pursuant to the Estimated Yield Formula ("Estimated Yield"). A Fixed Income UIT that includes a quotation of yield, or other similar quotation purporting to demonstrate the income to be earned or distributions to be made by the UIT, in its advertisements and sales literature would be required to include and give equal prominence to its Estimated Yield. The proposed amendments are intended to establish a uniform standard for calculating UIT yield to enhance the ability of prospective investors to make informed investment decisions.

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# I. Background

A UIT is a type of investment company that issues securities, typically called "units," representing undivided interests in a relatively fixed portfolio of securities.1 UITs are typically sponsored by broker-dealers, which assemble the UIT's portfolio securities, deposit the securities in a trust, and sell units of the UIT in a public offering. Unlike a mutual fund, a UIT does not have a board of directors or an investment adviser and its portfolio is not actively managed.

UIT units are redeemable securities that entitle an investor to receive his or her proportionate share of the UIT's net

assets upon redemption.

Notwithstanding this characteristic of UIT units, most UIT sponsors voluntarily maintain a secondary market for units of the UITs they sponsor.2 This secondary market reduces the frequency with which trusts are forced to liquidate as a result of unitholder redemptions.

UITs currently have approximately \$74 billion in aggregate assets, most of which (88 percent) are held by Fixed Income UITs.3 In marketing Fixed Income UITs to investors, sponsors and broker-dealers typically quote a rate of return that estimates the income that an investor who holds a unit for the expected life of the UIT can anticipate receiving. This method of marketing Fixed Income UITs is similar to the manner in which individual bonds are marketed to investors based on a bond's 'yield to maturity," 4 and may be contrasted to mutual fund performance marketing, which is based exclusively on the past performance of the mutual fund.5 The prominence of the

- <sup>1</sup> Section 4(2) of the 1940 Act [15 U.S.C. 80a-4(2)] defines a UIT as an investment company which (A) is organized under a trust indenture, contract of custodianship or agency, or similar instrument, (B) does not have a board of directors, and (C) issues only redeemable securities, each of which represents an undivided interest in a unit of specified securities. See generally Harman, Emerging Alternatives to Mutual Funds: Unit Investment Trusts and Other Fixed Portfolio Investment Vehicles, 1987 Duke L.J. 1045 (1987).
- <sup>2</sup>Sponsors that maintain secondary markets in the shares of the UITs they sponsor are considered issuers under section 2(4) of the 1933 Act [15 U.S.C. 77b(4)] and must comply with the registration requirements of the 1933 Act for units they offer to the public. In addition, under section 24(d) of the 1940 Act [15 U.S.C. 80a-24(d)], a broker-dealer selling UIT shares in the secondary market must comply with section 5(b) of the 1933 Act [15 U.S.C. 77e(b)] if the sponsor is continuing to sell shares in the trust
- <sup>3</sup> Source: Investment Company Institute. Tax-free debt securities represent approximately \$57 billion (89 percent) of the securities held by Fixed Income
- <sup>4</sup> Yield to maturity is the discount rate that equates the present value of future promised cash flows from the security to the current market price of the security. See W. Sharpe, Investments, 1028(5th ed. 1995).
- $^5$  See Item 22(b) of Form N-1A under the 1940 Act [17 CFR 274.11A], which specifies the manner in which mutual funds calculate yield and total