

August 5, 1971

To Our Clients:

Proposed Off-Shore Margin Loan Regulations. The FRB has proposed regulations to implement Title III of the Financial Recordkeeping and Currency and Foreign Transactions Reporting Act of 1970 designed to close the off-shore loan loophole illustrated by the MGM-Kerkorian case. The proposals make the margin regulations applicable to a U.S. or a U.S.-controlled borrower even though all the arrangements for the loan are made off-shore.

Foreign lenders who are U.S. persons, who are controlled by U.S. persons, or who act "on behalf of or in conjunction with" U.S. or U.S.-controlled persons, and make margin loans in the U.S. are made subject to the registration requirements of Regulation G with the New York FR Bank designated for such purpose.

The definition of "foreign person controlled by a U.S. person" in the proposed regulations is not precise. All 50% ownership situations are included. It is not clear whether U.S.-controlled entities with less than 50% U.S. ownership are also covered. Also left open is the question whether an off-shore fund with little or no U.S. ownership managed by a U.S. or U.S.-controlled investment adviser is included.

Tips, Tippees and Dinners. As expected, the SEC has affirmed the holding in Douglas Aircraft that a tippee cannot take advantage of the tip. The SEC holds that the tippee violates the law when:

- (1) the information is material and nonpublic,
- (2) the tippee knows or has reason to know the information is not public and has been obtained improperly, and

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- (3) the information is a factor in the decision to buy or sell.

The SEC holds information is material when it could be expected to affect the price if generally known. Information is obtained improperly when the tippee knows or has reason to know it was obtained by industrial espionage or commercial bribery or, depending on the facts, it is confidential. The tippee has the burden of proving that the information was not a factor in the decision to buy or sell.

The SEC specifically disclaimed that it would attach responsibility to information obtained by analysis or general observation.

As indicated, the SEC holding is not unexpected. It is an extension of the position taken in Cady Roberts and extended periodically since then. It gives rise to the opportunity to again warn -- Beware of dinners!

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