



NATIONAL CREDIT UNION ADMINISTRATION

WASHINGTON, D.C. 20456

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MAY 29 1985

Peter J. Germain, Esquire
Federated Investors, Inc.
Federated Investors Building
421 Seventh Avenue
Pittsburgh, PA 15219

Dear Mr. Germain:

This is in response to your letter of March 14, 1985, concerning Federal credit union (FCU) ~~valuation of trust and mutual fund investments.~~

As noted in your letter, in our letter dated April 24, 1984, we stated that, while at that time the valuation of a GNMA trust at acquisition cost without recognition of changes in market value was permissible, we were studying the issue. We have just completed our review of this matter. As more fully discussed below, we have concluded that FCU's must determine the net asset value of a share in a mutual fund (or trust) at the end of each accounting period, and adjust the investment to the lower of cost or market.

Unlike a direct investment in government securities, shares in a mutual fund or trust fund do not have a stated value at maturity date. The value of shares in such funds changes based on portfolio holdings and market conditions. Therefore, market conditions play a more significant role in determining the ultimate recoverable value of a fund than an investment with a specific maturity date. Generally accepted accounting principles and Section 2040.1.4 of the Accounting Manual for Federal Credit Unions require that marketable securities be recorded at the lower of cost or market on the balance sheet. The amount of the cost of the marketable security which represents the broker fee or commission, if any, may be added to the cost of the mutual or trust fund investment and recorded on the books as of the day of purchase. In addition, at the end of each accounting period, an FCU should determine the net asset value of a share in the trust or mutual fund and adjust the investment to the lower of cost or market.

Another issue has recently been brought to our attention concerning the involvement of trust and mutual funds in repurchase transactions. As stated in the prospectuses you submitted for the Federated Income Trust, the Federated Intermediate Government Trust and the Federated Short

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Intermediate Government Trust (Trusts), the Trusts may engage in repurchase transactions with banks or brokers. The prospectuses state that the Trusts or their custodians will take possession of the obligations subject to repurchase transactions. Our regulatory requirement for "investment-type" repurchase transactions (see 12 C.F.R. §703.2(1)(1)) will be satisfied in most instances because of the possession requirement of your Trusts. If, however, the Trusts are involved in repurchase transactions with their own custodians, where the custodians are the borrowers (receive monies from the Trusts for their securities and agree to repurchase the securities at a specified price and time), in order to satisfy the requirement of Section 703.2(1)(1), either the Trusts themselves must take possession of the securities or a third party custodian (a custodian not involved in the repurchase transaction) must hold the securities under a written bailment for hire contract, or the Trusts must be recorded as the owners of the securities through the Federal Reserve Book Entry System.

We hope that we have been of assistance.

Sincerely,

STEVEN R. BISKER
Assistant General Counsel