Securities-Based Lending – Video Transcript

"Securities-based lending" is the practice of allowing securities in an investment portfolio to serve as collateral for a loan, similar to the way a home serves as collateral for a home equity loan.

The main advantage of securities-based lending is investors get access to capital without having to sell any of their investment holdings.

Securities-based lending may be offered by banks, financial institutions, brokerages, and advisory firms. Securities that may be used as collateral include stocks, bonds, mutual funds, exchange-traded funds, and money market funds.

Here's how it typically works.

- The loan is commonly set up as a revolving line of credit.
- You can generally borrow between 50 and 95% of the value of your eligible securities, depending on the types of collateral you have and the value of the account.
- The securities used as collateral are deposited into a separate account – called a "pledged account" – and the lender becomes the lienholder. A lienholder has a *legal* claim to the account until the loan is repaid.
- You can continue to buy and sell securities in the pledged account.
- Interest-only payments on the loan are required each month.
- Some or all of the outstanding principal can be repaid at any time. The loan remains outstanding until the principal is repaid in full.

Securities-based lending has some key benefits.

- Not having to sell investments up front to obtain the loan helps you avoid potential capital gains taxes and allows you to continue to receive dividends, interest, and appreciation from your investments.
- Funds may be available quickly, usually within a week of signing the contract, and can be used for a variety of purposes.
- The interest rate on a securities-based loan is typically lower than some other forms of credit, including personal loans and credit cards.
- And the loan generally won't appear on your credit report.

But securities-based lending comes with risks:

- A market downswing or change in interest rates could happen at any time, which could make a securities-based loan less appealing.
- If interest rates rise, it could lead to a higher rate on your loan, depending on the type of loan you have.
- If the value of your pledged securities falls below a certain threshold, a "maintenance call" will require you to post additional collateral or repay the loan. Failure to do so allows the lender to sell your securities and keep the proceeds. This could lead to tax consequences.
- If you otherwise default on loan repayment, the lender can sell your securities.

Historically, securities-based lending was reserved for high-net-worth individuals, but today it's an option for investors with smaller portfolios. Before you consider a securities-based loan, make sure you fully understand the pros and cons.

Before obtaining a securities-based loan, you should fully understand that in a margin account you can lose more money than you have invested; you may have to deposit additional cash or securities in your account on short notice to cover market losses; you may be forced to sell some or all of your securities when falling securities prices reduce the value of your securities; and your brokerage firm may sell some or all of your securities without consulting you to pay off the loan it made to you.

All investments are subject to market fluctuation, risk, and loss of principal. When sold, investments may be worth more or less than their original cost.

Mutual funds and ETFs are sold by prospectus. Please consider the investment objectives, risks, charges, and expenses carefully before investing. The prospectus, which contains this and other information about the investment company, can be obtained from your financial professional. Be sure to read the prospectus carefully before deciding whether to invest.

Money market funds are neither insured nor guaranteed by the Federal Deposit Insurance Corporation (FDIC) or any other government agency. Although money market funds seek to preserve the value of your investment at $1.00 per share, it is possible to lose money by investing in such a fund.