List of Subjects in 17 CFR Part 250 and 259

Reporting and recordkeeping requirements, Public utility holding companies.

Text of Proposed Rule and Form Amendment

The Commission proposes to amend Parts 250 and 259 of Chapter II, Title 17 of the Code of Federal Regulations as set forth below:

PART 250—GENERAL RULES AND REGULATIONS, PUBLIC UTILITY HOLDING COMPANY ACT OF 1935

1. The authority citation for Part 250 continues to read in part as follows: Secs. 3, 20, 49 Stat. 810, 833; 15 U.S.C. 79c, 79t * * *.

2. By adding paragraph (f) to § 250.22 as follows:

§ 250.22 Applications and Declarations.

* * * * *

(f) *Proposed notice.* A proposed notice of the proceeding initiated by the filling of an application or a declaration shall accompany each application or declaration as an exhibit thereto and, if necessary, shall be modified to reflect any amendments to such application or declaration.

PART 259—FORMS PRESCRIBED UNDER THE PUBLIC UTILITY HOLDING COMPANY ACT OF 1935

§ 259.101 [Amended]

3. By amending General Instruction C of Form U–1 described in § 259.101 to read as follows:

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C. Attention is directed to the provisions of Rule 22 for certain additional procedural requirements, including the proposed notice requirement in Rule 22(f).

* * * * *

Regulatory Flexibility Act Certification

Pursuant to section 605(b) of the Regulatory Flexibility Act [5 U.S.C. 605(b)], the Chairman of the Commission has certified that the proposed amendments to Rule 22 and Form U–1 will not, if adopted, have a significant economic impact on a substantial number of small entities. This certification, including the reasons therefore, is attached to this release.

Dated: June 27, 1985.

By the Commission.

John Wheeler,

Secretary.

Regulatory Flexibility Act Certification

I, John S. R. Shad, Chairman of the Securities and Exchange Commission, hereby certify, pursuant to 5 U.S.C. 605(b), that the proposed amendments to Rule 22(f) and amended Form U–1 under the Public Utility Holding Company Act of 1935 ("Act") will not have a significant economic impact on a substantial number of small entities. The reason for this certification is as follows: Amended Rule 22(f) would require that all applications and declarations filed with the Commission pursuant to the Act include as an exhibit a proposed notice of the proceeding which is being initiated by the filing. Amended Form U–1 would refer persons using that form to the proposed notice requirement of Rule 22(f), and thus make the filing of proposed notices specifically applicable to such filings. The proposed notice would be patterned after the application or declaration being submitted and would require no additional information. Thus, the amendments would not have a significant economic impact upon applicants. Moreover, the definition of a small business as found in Rule 110 under the Act excludes all holding companies currently registered with the Commission.

Dated: June 27, 1985.

John S.R. Shad,

Chairman.

[FR Doc. 85–16131 Filed 7–8–85; 8:45 am]

BILLING CODE 8010–01–M

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17 CFR Part 270

[Release No. IC–14607; File No. S7–30–85]

Acquisition and Valuation of Certain Portfolio Instruments by Registered Investment Companies

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule and rule amendments.

SUMMARY: The Commission is proposing amendments to an existing rule that provides exemptive relief for money market funds to use the amortized cost method of valuing their portfolio securities or the penny-rounding method of computing their price per share. The proposed amendments would permit funds relying on the rule to acquire put options for liquidity purposes and to treat variable rate or floating rate debt securities with periodic demand features as short-term debt securities under certain conditions. The proposed amendments would also reduce the responsibilities which the existing rule assigns to money market fund directors and would allow money market funds to rely a high quality rating only if the rating is assigned by a nationally recognized statistical rating organization that is unaffiliated with the issuer of or with any insurer, guarantor or provider of credit support for the rated securities.

The Commission is also proposing amendments to an existing rule that exempts certain investment company acquisitions of securities issued by persons engaged in securities related businesses. The rule would be amended to permit money market funds to acquire liquidity puts from persons engaged in securities related businesses under certain conditions. Finally, the Commission is proposing a new rule that would provide exemptive relief to allow registered investment companies to assign a fair value of zero to certain types of put options, known as standby commitments, under certain conditions.

DATE: Comments must be received on or before September 9, 1985.

ADDRESS: Send comments in triplicate to John Wheeler, Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, D.C. 20549. (Reference to File No. (S7–30–85)). 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: Jack W. Murphy, Staff Attorney or Elizabeth K. Norsworthy, Chief, (202) 272–2048, Office of Regulatory Policy, Division of Investment Management, Securities and Exchange Commssion, 450 Fifth Street, NW., Washington, D.C. 20549.

SUPPLEMENTARY INFORMATION: The Securities and Exchange Commission today is asking for public comment on proposed amendments to rules 2a–7 [17 CFR 270.2a–7] and 12d3–1 [17 CFR 270.12d3–1] and on proposed rule 2a41–1 under the Investment Company Act of 1940 [15 U.S.C. 80a–1, *et seq.*] ("Act"). Rule 2a–7 permits, subject to specified conditions, certain open-end investment companies known as "money market funds" to use either (1) the amortized cost method of valuing their portfolio instruments [1] or (2) the penny-rounding

[1] A money market fund using the amortized cost method of valuation values its portfolio securities and other assets at acquisiton cost. The interest earned on each portfolio debt security (plus any discount received or less any premium paid upon purchase) is then accrued ratably over the remaining maturity of the security. By declaring these accruals to its shareholders as a daily dividend, the money market fund is able to set a fixed price per share, which is usually $1.00.

method of pricing their securities.[2] Rule 2a–7 requires money market funds using one of the above methods to limit their portfolio investments to instruments that are of high quality and that have a remaining maturity of one year or less. Funds relying on the rule must also maintain an average dollar-weighted portfolio maturity of no more then 120 days. Generally, the maturiy of an instrument is considered to be the maturity remaining on the face of the instrument. [3] However, the rule allows certain types of put options, known as "demand features," to be used to shorten the matrity of instruments that have variable or floating interest rates.[4]

The proposed amendments to rule 2a–7 would permit a money market fund relying on the rule to acquire put options for liquidity purposes only ("liquidity puts") under certain conditions. If adopted, the amendments would define "liquidity puts" to include demand features and "standby commitments," another type of put option that has been the subject of a number of prior exemptive orders. The proposed amendments would also permit funds relying on the rule to use periodic demand features to shorten the maturity of variable and floating rate instruments. In addition, the amendments would reduce the responsibilities related to the acquisition and disposition of demand feature instruments that the existing rule explicitly assigns to money market fund directors. The rule would also be amended to allow money market funds to rely on a high quality rating only if the rating is assigned by a nationally recognized statistical rating organization ("NRSRO") that is not affiliated with the issuer of, or with any insurer, guarantor or provider of credit support for the securities.[5]

The Commission is also proposing an amendment to rule 12d3–1 under the Act [17 CFR 270.12d3–1] to provide exemptive relief from section 12(d)(3) of the Act [15 U.S.C. 80a–12(d)(3)] to allow money market funds to acquire liquidity puts from persons engaged in securities related activities, under certain conditions. Finally, the Commission is proposing a rule under section 2(a)(41) of the Act [15 U.S.C. 80a–2(a)(41)] to allow registered investment companies to assign a fair value of zero to standby commitments under certain conditions.

Background

Rule 2a–7 codified prior exemptive orders permitting money market funds to use the amortized cost method of valuation or the penny-rounding method of pricing. At the time that the rule was adopted, the Commission discussed its application and scope in Investment Company Act Release No. 13380 (July 11, 1983) ("Release 13380"), [48 FR 32555]. In that release, the Commission stated that the rule did not address the acquisition or valuation of "puts or standby commitments" but suggested that these issues might be addressed in a future rule making process. The phrase "puts or stand-by commitments" was considered to encompass all agreements by a third party to purchase, at some future date and at a prescribed price, a security issued by another party.[6] For purposes of rule 2a–7, the Commission distinguished between puts running to a third party and demand features running to the issuer of the underlying security. This distinction was drawn due to the limited information regarding demand features that was available to the Commission staff and to the relatively undeveloped market in variable rate and floating rate instruments subject to those features that existed at the time rule 2a–7 was adopted.[7]

A. Market Changes

Since rule 2a–7 was adopted, a number of market changes have occurred that warrant a re-examination of the types of puts that may be used by money market funds to facilitate portfolio liquidity, including both third-party puts and issuer demand features, and the types of demand features that may be used to shorten the maturity of variable and floating rate instruments. The Commission also believes that market changes warrant amendment of rule 2a–7 to reflect industry practices regarding the role of money market fund directors in the making of decisions concerning demand feature instruments, and the circumstances under which a fund may rely on a high quality rating.

As noted above, rule 2a–7 prohibits money market funds relying on the rule from investing in most debt instruments which have a remaining maturity of more than one year or that will not be called for redemption within one year. However, the rule provides an exception for certain variable and floating rate instruments that are subject to demand features, a type of put option that runs to the issuer of the underlying instrument and allows the holder to obtain the principal amount of the instrument at any time upon no more than seven days' notice.[8] At the time that the rule was adopted, this exception provided a fair depiction of the types of variable and floating rate demand instruments that were available in the market and suitable for investment by funds relying on the rule.[9]

Over the past two years, however, new types of demand features have been developed, particularly with respect to variable or floating rate municipal securities. The Commission staff has been advised that these new demand features have been developed in order to avoid "reissuance" problems under the Internal Revenue Code of 1954 ("IRC"). Specifically, the Commission understands that when the holder of a municipal security exercises an issuer demand feature and the security is put back to the issuer or to a direct agent of the issuer, a subsequent remarketing of the security may constitute a reissuance of the security under the IRC.[10] When

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[2] A money market fund using the penny-rounding pricing method values portfolio securities for which market quotations are readily available at current market value, and other securities and assets at fair value as determined in good faith by the board of directors. The current net asset value per share is then rounded to the nearest one percent, allowing the fund to maintain a fixed price per share (usually $1.00). Penny-rounding funds also use the amortized cost valuation method to value portfolio securities having a remaining maturity of sixty days or less. *See* Investment Company Act Release No. 13380 (July 11, 1983), 48 FR 32555, at footnote 44, *citing* Investment Company Act Release No. 9786 (May 31, 1977), 42 FR 28999.

[3] Specifically, the rule provides that the maturity of an instrument shall be deemed to be the period remaining until the date noted on the face of the instrument as the date on which the principal amount owed must be paid, or in the case of an instrument called for redemption, the date on which the redemption payment must be made. *See* rule 2a–7(b)(3).

[4] Rule 2a–7 also allows a shorter maturity to be used in the case of variable interest rate instruments that are issued or guaranteed by the United States government or an agency thereof, or which are scheduled to be repaid in one year or less. *See* rule 2a–7(b)(5)(i) (A) and (C).

[5] The definition of "variable rate instrument" would also be changed to eliminate any confusion that may have arisen from the terminology used in the present definition, and references to the amortized cost and penny-rounding methods modified to describe these methods more precisely. Further, the parenthetical references in the rule to "trustees" would be eliminated since the definition of "director" in section 2(a)(12) of the Act [15 U.S.C. 80a–2(a)(12)] specifically includes a member of a board of trustees.

[6] *See* footnote 9 of Release 13380 and accompanying text.

[7] The rule's provision that permits a fund to treat variable and floating rate instruments with demand features as short-term debt securities under certain conditions went beyond a codification of exemptive orders previously issued. *See* footnote 16 of Release 13380 and accompanying text.

[8] *See supra* note 4, discussing other exceptions to the one year remaining maturity requirement of present rule 2a–7.

[9] *See* footnote 20 of Release 13380, *citing* letter from Gerald Osheroff, Associate Director, Division of Investment Management to Joel T. Matcovsky, Merrill Lynch Asset Management, Inc., dated December 10, 1981.

[10] Many municipal securities that are subject to demand features have variable interest rates. When

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this occurs, a municipal issuer may be forced to requalify the security as tax-exempt prior to remarketing it. Moreover, under the amended tax code, the remarketed security may no longer qualify as tax-exempt.

The Commission understands that, in order to avoid the possibility of a reissuance, issuers of municipal securities have begun to structure demand features that do not run directly to the issuer or its agent, but run, in the first instance, to a separate entity that is provided with sufficient third-party credit support to honor the demands.[11] The securities that are put to the separate entity are then remarketed without ever having entered into the possession of the issuer or a direct agent of the issuer. By so structuring the demand feature, the issuer is able to make a more convincing argument that the remarketing of the securities is nothing more than a secondary market transaction and not a reissuance of the securities.

Another market development that has been brought to the Commission's attention is the growth of demand features that give the holder of the underlying debt instrument the right to recover the principal amount of the instrument at specified intervals (*i.e.*, quarterly, semi-annually, etc.) ("periodic demand features").[12] As noted above, the rule 2a–7 currently permits funds relying on the rule to treat as short-term debt securities floating rate or variable rate instruments with demand features that give the holder the right to recover the principal amount of the underlying securities upon no more than seven days' notice ("seven-day demand instruments"). The Commission understands that variable and floating rate instruments are now being marketed with periodic demand features because the cost of servicing these features is lower than the cost of servicing seven-day demand features. As is the case with seven-day demand instruments, it appears that the market values instruments with periodic demand features essentially as short-term debt securities having a maturity equal to the time remaining until a demand may be made or the interest rate adjusted.

The Commission also understands that, at least at the present time, it is primarily municipal securities that are being marketed as variable or floating rate instruments with these demand features. The limitations of the present rule are, therefore, felt most acutely by money market funds that limit their investments to municipal securities ("municipal funds"). As the number of municipal funds has increased,[13] and more variable or floating rate instruments are marketed with third party demand features or periodic demand features, the supply of demand feature instruments that satisfy the existing rule has contracted fairly dramatically.[14] Without a rule amendment, municipal funds will be excluded from a significant segment of the municipal securities market and may be forced to accept a lower yield on their investments.

The Commission's staff has been advised that at least 50% of the securities in municipal fund portfolios are variable or floating rate instruments.[15] Yet, under the existing rule, a fund's board of directors is assigned the responsibility of deciding whether the fund may acquire a variable or floating rate instrument with a demand feature and whether the fund may continue to hold that instrument.[16] Release 13380 permits the directors to delegate these responsibilities, and the Commission understands that this is invariably the case, given the degree to which funds are now investing in demand feature instruments. The Commission believes, therefore, that the rule should be amended to remove these director determinations and provide objective standards.

As noted above, rule 2a–7 conditions exemptive relief upon the quality of the debt instruments that are in a fund's portfolio. The rule states that each portfolio security must have a high quality rating from a major rating service or be determined to be of comparable quality by the board of directors. The Commission believes that the rule's references to "major rating service" should be changed to refer to "nationally recognized statistical rating organization" ("NRSRO"), the term that is used elsewhere in rules and regulations under the federal securities laws.[17] The Commission also believes that a fund should rely on a high quality rating only if the NRSRO is unaffiliated with the issuer of the securities and with any insurer, guarantor or provider of credit support for the securities.

B. Acquisition and Valuation of Standby Commitments

When rule 2a–7 was issued, the Commission's experience with puts on debt instruments that ran to third parties was largely limited to a type of put referred to as a "standby commitment." Beginning in 1981, the Commission began to receive and grant applications for exemptive relief from investment companies issuing redeemable securities, (*i.e.*, open-end management companies and unit investment trusts) to allow those companies to acquire standby commitments for municipal securities from brokers, dealers and other financial institutions in order to facilitate portfolio liquidity. The applicants also requested exemptive relief to allow such standby commitments to be assigned a fair value of zero.[18] All of the applicants have been

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the demand is exercised by a holder, the security will often be remarketed by a remarketing entity, which will adjust the interest rate to make the security more attractive to potential buyers. The remarketing entity is generally limited to choosing a new interest rate within a certain number of basis points above or below a stated index. In a tax context, the ability of the remarketing entity to set a new interest rate, coupled with a demand feature that requires the security to be put back to the issuer or to a direct agent of the issuer, could create the appearance that the remarketed security is a fundamentally different instrument from the original security. Under such circumstances, the remarketing of the security could be deemed a reissuance under the tax law. *See generally*, Winterer, *"Reissuance" and Deemed Exchanges Generally*, 37 Tax Lawyer 509 (1984).

[11] Avoiding the appearance of a reissuance has always been a factor in the structuring of municipal debt issues subject to demand features. However, the extensive changes in the tax code in recent years have made it increasingly difficult for a pre-existing municipal issue to requalify as tax-exempt. Therefore, municipal issuers have become even more wary of structuring demand features that would create the appearance that remarketed securities are reissued securities. *Id.*

[12] Tax considerations have also caused periodic demand features on municipal securities to be structured to run to a third party. *See supra* notes 10–11 and accompanying text.

[13] In 1982 there were 37 municipal money market funds. By the end of 1983, the number had increased to 66 funds. As of April 19, 1985, there were 92 municipal money market funds in existence, managing some $34 billion in assets.

[14] The supply of such instruments has been further reduced by the withdrawal from the tax-exempt note market of project notes issued by local housing authorities and marketed by the Department of Housing and Urban Development. ("HUD"). In 1983, total borrowings through project notes totalled $18.42 billion. However, the Deficit Reduction Act of 1984 cast doubt on the tax-exempt status of project notes. As a result, new issues of project notes were halted in August, 1984 and the total volume of such borrowings for 1984 totalled only $11.57 billion. This reduction was partially responsible for a reduction in total short-term tax exempt borrowings in 1984 to $30.54 billion, from the 1983 total of $35.85 billion.

[15] As noted *Supra* in footnote 13, as of April 19, 1985, the total assets of municipal money market funds equalled $34 billion. At least $17 billion of those assets are in demand feature instruments.

[16] *See* rule 2(a)(7)(b)(5) (i) and (ii).

[17] *See* discussion *infra* re rating services.

[18] Generally, the applicants have sought exemptive relief from sections 12(d)(3) and 2(a)(41) of the Act and from rules 2a–4 and 22c–1 under the Act.

municipal funds[19] and, with few exceptions, [20] all have been money-market funds that use the amoritized cost valuation method.

In their applications, the municipal funds have represented that they are continually faced with unique liquidity problems. As in the case of other investment companies issuing redeemable securities, municipal funds must maintain a level of portfolio liquidity that is sufficient to meet redemption requests. However, unlike other funds, municipal funds frequently purchase municipal securities pursuant to delayed delivery contracts.[21] When purchasing securities on a delayed delivery basis, a fund is required to maintain, in a segregated account, liquid assets equal to the purchase price due at settlement.[22]

The applicants have also represented that, because municipal securities usually have a limited range of maturity dates, municipal funds have greater difficulty than other types of funds in assembling a portfolio with securities that mature daily. Consequently, a municipal fund is ofter forced to sell a portion of its portfolio in order to meet redemptions, to retain investment flexibility and to maintain adequate coverage in its segregated accounts.

According to the applicants, the secondary market for certain types of municipal securities is more limited than that for other types of debt instruments. Where a fund holds in its portfolio fixed rate short-term municipal paper, the fund may often have problems selling the paper prior to maturity.[23] Applicants have represented that municipal securities dealers generally tender bids on a transactional basis, and do not continually make a market in the securities. Moreover, achieving same-day settlement on a secondary market sale may often entail a fund accepting a less favorable price for the municipal securities being sold.

As a result of the above liquidity problems, the applicants have maintained that when a fund purchases short-term fixed rate municipal securities from a broker, dealer or other financial institution, it is often in the fund's best interest to acquire at the same time a "standby commitment" allowing the fund to put the securities back to the seller at an agreed-upon price or yield prior to maturity. The exercise price of such commitments equals the amortized cost of the underlying securities at the time of exercise, plus accrued interest, if any. The applicants have represented that the standby commitments will not be used to affect the value of the underlying securities.

According to applicants, municipal funds usually pay nothing or only a nominal consideration for standby commitments.[24] The applicants have stated that the commitments will be exercised only as a last resort, because the broker, dealer or other financial institution would suffer a loss on the transaction if the exercise price is greater than the market value of the underlying securities at the time of exercise. According to applicants, if the broker or dealer suffers a loss on the transaction, the fund is unlikely to acquire any standby commitments from that broker or dealer in the future. Since it is difficult to evaluate whether a standby commitment will ever be exercised, or, if it is exercised, whether the fund will benefit from the transaction, applicants have requested exemptive relief to assign a fair value of zero to the commitments, with any consideration paid to be accounted for as unrealized depreciation.

So that municipal funds will no longer have to file applications for exemptive relief in order to acquire standby commitments, in addition to amending rule 2a-7, the Commission is also proposing an amendment to rule 12d3-1. The proposed amendment would allow a money market fund to acquire standby commitments and other liquidity puts for persons engaged in securities related activities, provided that the fund complies with the conditions of rule 2a-7. The Commission is also proposing rule 2a41-1 to give investment companies exemptive relief to assign a fair value of zero to standby commitments under certain conditions that are based on the prior exemptive orders.

Discussion

A. Amendments to rule 2a-7

1. *Liquidity puts.* As noted above, rule 2a-7 presently allows a money market fund to use either the amortized cost valuation method or the penny-rounding pricing method to maintain a fixed price per share, provided that the fund complies with certain conditions. These conditions include (1) limiting portfolio investments to high quality instruments having a remaining maturity, as determined in accordance with the rule, of one year or less; and (2) maintaining a dollar-weighted average portfolio maturity not exceeding 120 days. The quality and maturity requirements of the rule are designed to ensure that the fixed price per share accurately reflects the fund's actual net asset value per share.[25]

As discussed above, since the adoption of rule 2a-7, a number of changes have occurred in the types of short-term money market instruments available for purchase.[26] The proposed

[19] Since 1981, at least 60 applications have been filed, and the requested relief granted. *See, e.g.*, Cash Accumulation Trust, Investment Company Act Release Nos. 14177 (October 1, 1984) [49 FR 39256] and 14218 (October 30, 1984); Financial Tax-Free Money Fund, Inc., Investment Company Act Release Nos. 13444 (August 18, 1983) [48 FR 38564] and 13503 (September 13, 1983); Tax-Exempt Money Market Fund, Investment Company Act Release Nos. 12508 [June 25, 1982] [47 FR 29041] and 12552 (July 22, 1982) and Municipal Fund for Temporary Investment, Investment Company Act Release Nos. 11822 (June 19, 1981) [46 FR 33151] and 11887 (July 21, 1981).

[20] *See e.g.*, Hutton Municipal Fund, Inc., Investment Company Act Release Nos. 13154 (April 12, 1983) [48 FR 17006] and 13229 (May 10, 1983), and Security Tax Exempt Fund, Investment Company Act Release Nos. 13656 (December 6, 1983) [48 FR 55377] and 13898 (January 5, 1984).

[21] By the terms of this type of contract, the fund makes a firm commitment to purchase securities that will be delivered at a later date.

[22] *See* Investment Company Act Release No. 10666 (April 18, 1979) [44 FR 25128] in which the staff of the Division of Investment Management took the position that any firm commitment to purchase securities on a delayed delivery basis would be considered a senior security. Although section 18(f) [15 U.S.C. 80a-18(f)] of the Act does not permit an open-end investment company to issue senior securities, the staff stated that it would not recommend enforcement action if a company maintains liquid assets in a segregated account equal in value to the purchase price due on the settlement date.

[23] Many of the applications have involved standby commitments on project notes issued by local housing authorities and marketed through the Department of Housing and Urban Development. As discussed in footnote 13, *supra*, new issues of project notes were discontinued in August, 1984. However, the Commission has continued to receive applications since that date that refer to standby commitments on other types of municipal securities.

[24] Applicants have represented that the total amount of consideration paid for standby commitments will not exceed ½ of 1% of the value of their total assets, as calculated immediately after acquisition.

[25] Fluctuations in the market value of the portfolio of a money market fund utilizing amortized cost or penny-rounding could result in a net asset value per share that is either higher or lower than the fixed price per share. There are basically two types of risk which cause fluctations in the value of money market fund portfolio instruments: the market risk, which primarily results from fluctuations in the prevailing interest rate, and the credit risk. In general, instruments with shorter periods remaining until maturity have reduced market risks and thus tend to fluctuate less in value over time than instruments with longer periods remaining until maturity. Similarly, instruments which are of higher quality have lower credit risks and tend to fluctuate less in value over time than instruments which are of lower quality.

[26] While the market changes that have occurred have primarily involved the short-term municipal securities market, the proposed amendments to rule 2a-7 would be applicable to all money market funds.

amendments would address these market changes by amending the rule to allow money market funds to acquire put options for liquidity purposes ("liquidity puts") and to use periodic demand features to shorten the maturity of variable and floating rate instruments. The proposed amendments would also reduce the responsibilities which the existing rule assigns to money market fund directors and would allow money market funds to rely on a high quality rating only if the rating is assigned by a NRSRO that is unaffiliated with the issuer of or any insurer, guarantor or provider of credit support for the securities.[27]

The proposed amendments would define a "liquidity put" as a right to sell a specified underlying security or securities within a specified period of time at a certain exercise price. This definition would specifically include standby commitments that entitle the holder to achieve same day settlement and that have an exercise price equal to the amortized cost of the underlying security or securities plus accrued interest, if any, at the time of exercise. The definition would also include demand features that allow the holder to receive the principal amount of the underlying security or securities plus accrued interest, if any, at the time of exercise, either at any time upon no more than seven days' notice or at specified intervals not exceeding one year and upon no more than seven days' notice. To ensure that these options are acquired only to facilitate portfolio liquidity, the proposed definition would state that a liquidity put may be sold, assigned or otherwise transferred only in conjunction with a sale or transfer of the underlying security or securities.

The amended rule would limit the liquidity puts that a fund may acquire from any one institution. The value of the securities underlying all liquidity puts from the same institution would be limited to five percent of the total value of the fund's portfolio. In case of a fund using the amortized cost valuation method, the total value of the fund's assets would be calculated using the amortized cost of the fund's assets portfolio instruments; in the case of a fund using the penny-rounding pricing method, the total value would be calculated using the market or fair value of the fund's portfolio securities. If adopted, this limitation would prevent a money market fund from relying too heavily upon any one institution to maintain the fund's portfolio liquidity and would supercede the conditions of prior exemptive orders.

The amended rule would require that any liquidity put must satisfy the same high quality standard that is applied to other portfolio securities.[28] Therefore, a standby commitment or a demand feature would have to present minimal credit risks as determined by the board of directors and have received a rating of high quality or, if unrated, be of comparable quality as determined by the fund's board of directors or trustees.[29]

2. *Demand features.* The proposed amendments to rule 2a–7 would allow money market funds to uses periodic demand features, as well as seven-day demand features, to shorten the maturity of underlying securities that have variable or floating interest rates. The amendments would also remove the requirement that a demand feature must run to the issuer of the underlying security or securities.[30] By making these changes, the Commission intends to allow the issuers of variable and floating rate demand instruments[31] to market these securities to money market funds, while retaining maximum flexibility in structuring the put mechanism.

The proposed amendments would allow a fund to use a shorter maturity for a variable or floating rate demand instrument.[32] only if both the long-term and short-term credit aspects of the demand instrument are of high quality.[33] In determining the quality of a demand instrument, the fund may rely on a high quality rating assigned by an unaffiliated NRSRO[34] if the rating organization has considered both the long-term and short-term aspects of the instrument.[35] If only one aspect of the instrument has been rated, or where neither aspect has been rated, the board of directors may determine that any unrated aspect of the instrument is of a quality comparable that of similar instruments which have high quality short-term and long-term ratings.[36]

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[27] If the proposed amendments are adopted, the adopting release would serve as the operative interpretive vehicle for those parts of rule 2a–7 that are amended. Release 13380 would continue to serve as the operative interpretive vehicle for the provisions of rule 2a–7 which remain substantively unchanged.

[28] *See* rule 2a–7 (a)[iv) *and* (b)[iii) and discussion *infra*.

[29] In determining whether an unrated standby commitment, demand feature or other liquidity put is of comparable quality, the fund's board of directors should, of course, examine all relevant data. Examples of relevant data would include such factors as the creditworthiness of the party responsible for paying the exercise price when the put is exercised and the credit support (such as a letter of credit, insurance, or other backup arrangement), if any, provided to ensure timely payment on the put.

[30] The Division of Investment Management has interpreted that provision to mean that a demand feature may also run to an agent of the issuer. *See* letter from Gerald Osheroff, Associate Director, to the Honorable Lee Sherman Dreyfus, Governor of Wisconsin, dated October 22, 1982 (publicly available March 3, 1983).

[31] A variable rate instrument would be redefined as one whose terms provide for the adjustment of its interest rate on set dates and which, upon such adjustment, can reasonably be expected to have a market value that approximates its par value. This definition removes the requirement in the present rule that the adjustment of the interest rate be "automatic" (*see* rule 2a–7(b)[3)]. The Commission staff has been informed that the "automatic" terminology of the present rule has caused some confusion in the industry. Many variable rate instruments are structured so that on the date when the interest rate is scheduled to be adjusted, the interest rate is usually changed by a remarketing agent to a new rate which reflects current market rates. Since the remarketing agent often has discretion to set the rate within a given number of basis points above or below an appropriate index of current interest rates uncertainty has arisen as to whether the interest rate adjustment is "automatic" within the meaning of the rule. The proposed amendments would eliminate any confusion resulting from the use of the term "automatic" in the present definition, in order to make it explicit that where the interest rate of an instrument is adjusted in a manner similar to that described above, the instrument would still be considered a variable rate instrument under this rule.

[32] The maturity of a variable rate demand instrument would, under the amendments, be determined in the same manner that is currently used to determine the maturity of such an instrument under the rule. Similarly, the maturity of a floating rate demand instrument would be determined in the same manner as currently used to determine the maturity of that type of instrument under the rule.

[33] The quality of a demand instrument depends both upon the ability of the issuer of the underlying security to meet scheduled payments of principal and interest and upon the availability of sufficient liquidity to allow a holder of the instrument to recover the principal amount upon exercise of the demand feature. Therefore, the demand instrument combines both long-term and short-term credit risk. In recognition of the dual nature of the credit risks pertaining to such instruments, at least two major rating agencies have begun to assign dual ratings to demand instruments.

[34] *See* discussion *infra* regarding rate agencies.

[35] If both the long-term and short-term credit aspects have been considered, the money market fund may rely on a single high quality rating assigned by a NRSRO.

[36] In determining whether an unrated unlerlying security of a demand feature is of comparable quality, it is anticipated that the board would examine the instrument in a manner similar to that used for securities that are not subject to a demand feature. However, if the demand feature runs to the issuer of the underlying security or if the issuer is ultimately responsible for honoring the demand feature, the board should also examine the effect, if any, that the existence of the demand feature would have on the issuer's long-term creditworthiness. Similarly, in examining the demand feature itself, the board should examine typical short-term credit factors including the existence of sufficient liquidity to enable the principal amount to be recovered in a timely fashion once the demand is made. Such liquidity, of course, may depend upon the short-time creditworthiness of the party responsible for honoring the demand or upon third party credit support agreements such as letters of credit or insurance, or upon a combination of these factors.

There may be situations where a security has been rated by a NRSRO that did not consider the existence of an external agreement to provide credit support, such as a letter of credit from a bank or an insurance policy. Under those circumstances, the fund may consider the security to be an unrated security and the board, taking into account the external agreement, may determine that the security is of comparable quality.[37] Where the instrument has received different ratings from different rating organizations, the rule's requirements would be satisfied if a high quality rating for each aspect has been received from at least one NRSRO.[38]

In the event that either the long-term or the short-term rating of the demand instrument were to fall below high quality or comparable quality as determined by the fund's board of directors, the proposed amendments would require the fund to treat the underlying security as having the maturity indicated on the face of the instrument. If the remaining maturity were in excess of one year, the fund would have to dispose of the underlying security within a reasonable time and in a manner best suited to the fund's interests, whether by exercising the demand feature or by selling the instrument on the secondary market.[39]

Under the present rule, if a money market fund intends to use a demand feature to shorten the maturitry of a variable rate instrument, its board of directors must first determine that whenever a new interest rate is established, it is reasonable to expect that the instrument will have a current market value that approximates its par value.[40] A similar determination is required for a floating rate instrument.[41] Under the amended rule, the directors would no longer have to make these determinations. Instead, these standards would be incorporated into the definitions of variable rate and floating rate instruments.[42]

Under the present rule, the directors are also required to make a quarterly determination that the demand feature instrument is still of high quality.[43] The Commission believes that the directors do not need to be involved in routine quality determinations where the demand feature instrument has a dual high quality rating from an unaffiliated NRSRO. Under the amended rule, fund directors would no longer have the day-to-day responsibility of determining whether the fund should acquire and continue to hold a demand feature instrument, unless the short-term or long-term aspects of the instrument are unrated. In that case, as is the case with any unrated debt security under the rule, the directors would have to determine that the instrument is of comparable quality.

3. *Rating services.* As noted above, rule 2a–7 presently requires that a money market fund limit its portfolio investments to instruments that have received a high quality rating from any major rating service or which are of comparable quality as determined by the fund's board of directors. To conform rule 2a–7 to other rules and regulations under the federal securities laws, [44] the proposed amendments would replace references to a "major rating service" with references to a "nationally recognized statistical rating organization (NRSRO")," as that term is used in the Commission's net capital rule.[45] The amended rule would allow money market funds to rely on a high quality rating assigned by a NRSRO only if the rating organization is unaffiliated with the issuer of, and any insurer, guarantor or provider of credit support (e.g. letters of credit) for, the rated securities. Although the concept of independence is implicit in the term NRSRO, the Commission believes that, for the purposes of rule 2a–7, independence should be defined within the context of the Act. Accordingly, the amended rule would require that a NRSRO may not be an "affiliated person"; of the issuer of, or any insurer, guarantor or provider of credit support for, the rated securities. The term "affiliated person" is defined in section 2(a)(3) of the Act [15 U.S.C. 80a–2(a)(3)].

B. Proposed Amendment to Rule 12d3–1

Section 12(d)(3) of the Act (15 U.S.C. 80a–12(d)(3)] prohibits any registered investment company and any company or companies controlled by such registered investment company from purchasing or otherwise acquiring any security issued by or any other interest in the business of any person who is a broker, a dealer, an investment adviser to an investment company, an investment adviser registered under the Investment Advisers Act of 1940 [15 U.S.C. 80b–1 *et seq.*] or who is engaged in the business of underwriting (collectively "securities related businesses"). The Commission recently adopted revised rule 12d3–1 under section 12(d)(3) to enable registered investment companies to acquire securities issued by persons engaged in securities related businesses under certain conditions.[46] That revised rule provides a blanket exemption for investment company acquisitions of the securities of issuers that derive 15% or less of their gross revenues from securities related activities, and a conditional exemption for the acquisition of securities of issuers deriving more than 15% of their gross revenues from such activities.

As noted above, municipal funds must obtain exemptive relief from section 12(d)(3) to acquire standby commitments from persons engaged in securities related businesses. So that money market funds will no longer have to file applications for exemptive relief to acquire standby commitments or other types of liquidity puts, the Commission is proposing an amendment to rule 12d3–1 that would allow these acquisitions, provided that the acquiring company complies with rule 2a–7 as amended. This would permit a money market fund to acquire standby commitments and demand features from persons engaged in securities related activities, as long as the value of the securities underlying the puts from any one institution does not exceed 5% of the total value of the fund's portfolio and as long as the liquidity puts meet the quality conditions of rule 2a–7. The amended rule would supersede prior exemptive orders.

C. Proposed Rule 2a41–1

As discussed above, since it is difficult to evaluate whether a standby

[37] *See* Release 13380, footnotes 34–35.

[38] *Id.*

[39] *See* Release 13380, footnote 22. Of course, if the remaining maturity of the underlying security were less than one year, or if the redemption date were within one year, the fund could continue to hold the underlying security and assign a maturity equal to the remaining maturity or the period until the redemption date.

[40] *See* rule 2a–7(b)(5)(i)

[41] In the case of a floating rate instrument, the board must determine that it is reasonable to expect that the floating rate feature will ensure that the market value of the instrument will always approximate its par value. *See* rule 2a–7(b)(5)(ii)(A).

[42] Of course, the amended rule would not alter the responsibility of the board of directors to monitor the performance of the fund's investment adviser. This responsibility would continue to include the duty to review and monitor the appropriateness of the standards used by the adviser in making determinations concerning the purchase, retention and disposition of variable and floating rate demand instruments.

[43] *See* rule 2a–7 (b)(5)(i)(B) *and* (b)(5)(ii)(B).

[44] *See, e.g.*, rule 134 [17 CFR 230.134] under the Securities Act of 1933 [15 U.S.C. 77a *et seq.*], the general instructions to regulation S–K under that Act [17 CFR 229.10] and the eligibility requirements for use of form S–3 under that Act [17 CFR 239.13].

[45] *See* rule 15c3–1(c)(2)(vi)(F) [17 CFR 240.15c3–1(c)(2)(iv)(F)] under the Securities Exchange Act of 1934 [15 U.S.C. 78a *et seq.*]

[46] *See* Investment Company Act Release No. 14036 (July 13, 1984) [49 FR 29362] adopting the revised rule.

commitment will ever be exercised or, if it is exercised, whether the fund will benefit from the transaction, a number of municipal funds have requested and received exemptive relief to assign a fair value or zero to these instruments. Proposed rule 2a41–1 would allow an investment company's board of directors to make this fair value determination as long as the standby commitment is not used to affect the value of the underlying security or securities and as long as any consideration paid for the standby commitment is accounted for as unrealized depreciation. For example, a money market fund relying on the rule could not use the standby commitment to affect the market value of the underlying securities for purposes of monitoring any deviation between the fixed price per share and its current value per share. The rule, if adopted, would supersede prior exemptive order.[47]

Request for Comment

The Commission is requesting general comment on any other issues relating to rule 2a–7 or the acquisition and use of put options by registered investment companies that have not been addressed in this release.

List of Subjects in 17 CFR Part 270

Investment companies, Reporting and recordkeeping requirements, Securities.

Statutory Basis and Text of Proposed Rule Amendments

The proposed amendments to rules 2a–7 and 12d3–1 and proposed rule 2a41–1 would be adopted pursuant to the authority granted the Commission in sections 6(c) [15 U.S.C. 80–6(c)], 22(c) [15 U.S.C. 80a–22(c)] and 38(a) [15 U.S.C. 80a–37(a)] of the Act.

PART 270—RULES AND REGULATIONS, INVESTMENT COMPANY ACT OF 1940

Part 270 of Chapter II of Title 17 of the Code of Federal Regulations is amended as shown.

1. The authority citation for Part 270 continues to read in part as follows:

Authority: Secs. 38, 40, 54 Stat. 841, 842, 15 U.S.C. 80a–37 80c–89 * * *

2. By revising paragraphs (a)(1), (a)(2)(i), (ii), and (iv), revising and redesignating (a)(2)(v) as (vi), redesignating (a)(2)(vi) as (vii), adding a new paragraph (a)(2)(v), revising (a)(3)(i) and (iii), adding (a)(3)(iv), revising paragraph (b) and adding paragraph (c) of § 270.2a–7 as follows:

§ 270.2a–7 Use of the amortized cost valuation and penny-rounding pricing methods by certain money market funds.

(a) * * *

(1) The board of directors of the money market fund determines, in good faith based upon a full consideration of all material factors, that it is in the best interest of the fund and its shareholders to maintain a fixed price per share, by using the amortized cost method of valuation or the penny-rounding method of pricing, and that the money market fund will continue to use such method or methods only so long as the board of directors believes that it fairly reflects the market based net asset value per share; and either

(2) * * *

(i) In supervising the money market fund's operations and delegating special responsibilities involving portfolio management to the money market funds's investment adviser, the money market fund's board of directors undertakes—as a particular responsibility within the overall duty of care owed to its shareholders—to establish procedures reasonably designed, taking into account current market conditions and the money market fund's investment objectives, to assure to the extent reasonably practicable that the fund's price per share, as computed for the purpose of distribution, redemption and repurchase, fairly reflects the market based net asset value per share.

(ii) Included within the procedures to be adopted by the board of directors shall be the following:

(A) Procedures adopted whereby the extent of deviation, if any, of the current net asset value per share calculated using available market quotations (or an appropriate substitute which reflects cufrent market conditions) from the money market fund's amortized cost price per share, will be determined at such intervals as the board of directors deems appropriate and are reasonable in light of current market conditions; periodic review by the board of directors of the amount of the deviation as well as the methods used to calculate the deviation; and maintenance of records of the determination of deviation and the board's review thereof,

(B) In the event such deviation from the money market fund's amortized cost price per share exceeds ½ of 1 percent, a requirement that the board of directors will promptly consider what action, if any, should be initiated by the board of directors, and

(C)Where the board of directors believes the extent of any deviation from the money market fund's amortized cost price per share may result in material dilution or other unfair results to investors or existing shareholders, it shall take such action as it deems appropriate to eliminate or reduce to the extent reasonably practicable such dilution or unfair results.

* * * * *

(iv) The money market fund will limit its portfolio investments, including liquidity puts and repurchase agreements, to those United States dollar-denominated instruments which the board of directors determines present minimal credit risks and which are of "high quality" as determined by any unaffiliated nationally recognized statistical rating organization or, in the case of any instrument that is not rated, of comparable quality as determined by the board directors;

(v) Immediately after the acquisition of any liquidity put, the money market fund will not have invested more than 5 percent of the total amortized cost value of its assets in securities underlying liquidity puts from the same institution;

(vi) The money market fund will record, maintain, and preserve permanently in an easily accessible place a written copy of the procedures (and any modifications thereto) described in paragraph (a)(2)(i) of this section and the money market fund will record, maintain, and preserve for a period of not less than six years (the first two years in an easily accessible place) a written record of the board of directors' considerations and actions taken in connection with the discharge of its responsibilities, as set forth above, to be included in the minutes of the board of directors' meetings. The documents preserved pursuant to this condition shall be subject to inspection by the Commission in accordance with section 31(b) of the Act [15 U.S.C. 80a–30(b)] as if such documents were records required to be maintained pursuant to rules adopted under section 31(a) of the Act [15 U.S.C. 80a–30(a)];

* * * * *

(3) * * *

(i) In supervising the money market fund's operations and delegating special responsibilities involving portfolio management to the money market fund's investment adviser, the money market fund's board of directors undertakes—as a particular responsibility within the overall duty of care owed to its shareholders—to assure to the extent

[47] If the proposed rule is adopted, the Commission proposes to give notice to all funds with standby commitment exemptive orders of its intention to amend those orders to bring them into conformity with the rule.

reasonably practicable, taking into account current market conditions affecting the money market fund's investment objectives, that the money market fund's price per share as computed for the purpose of distribution, redemption and repurchase, fairly reflects the market-based net asset value per share.

* * * * *

(iii) The money market fund will limit its portfolio investments, including liquidity puts and repurchase agreements, to those United States dollar-denominated instruments which the board of directors determines present minimal credit risks and which are of "high quality" as determined by any unaffiliated nationally recognized statistical rating organization, or, in the case of an instrument that is not rated, of comparable quality as determined by the board of directors.

(iv) Immediately after the acquisition of any liquidity put, the money market fund will not have invested more than 5 percent of the total market-based value of its assets in securities underlying liquidity puts from the same institution.

(b) For the purposes of this rule, the maturity of a portfolio instrument shall be deemed to be the period remaining until the date noted on the face of the instrument as the date on which the principal amount owed must be paid, or in the case of an instrument called for redemption, the date on which the redemption payment must be made, except that:

(1) An instrument that is issued or guaranteed by the United States government or any agency thereof which has a variable rate of interest readjusted no less frequently than annually may be deemed to have a maturity equal to the period remaining until the next readjustment of the interest rate.

(2) A variable rate instrument, the principal amount of which is scheduled on the face of the instrument to be paid in one year or less, may be deemed to have a maturity equal to the period remaining until the next readjustment of the interest rate.

(3) A variable rate instrument that is subject to a demand feature may be deemed to have a maturity equal to the longer of the period remaining until the next readjustment of the interest rate or the period remaining until the principal amount can be recovered through demand, as long as such demand instrument continues to receive a short-term and a long-term high quality rating from an unaffiliated nationally recognized statistical rating organization or, if not rated, is determined to be of comparable quality by the board of directors.

(4) A floating rate instrument that is subject to a demand feature may be deemed to have a maturity equal to the period remaining until such principal amount can be recovered through demand, as long as such demand instrument continues to receive a short-term and a long-term high quality rating from an unaffiliated nationally recognized statistical rating organization or, if not rated, is determined to be of comparable quality by the board of directors.

(5) A repurchase agreement may be deemed to have a maturity equal to the period remaining until the date on which the repurchase of the underlying securities is scheduled to occur, or where no date is specified, but the agreement is subject to demand, the notice period applicable to a demand for the repurchase of the securities.

(6) A portfolio lending agreement may be treated as having a maturity equal to the period remaining until the date on which the loaned securities are scheduled to be returned, or where no date is specified, but the agreement is subject to demand, the notice period applicable to a demand for the return of the loaned securities.

(c) *Definitions.* (1) The "amortized cost method of valuation" is the method of calculating an investment company's net asset value whereby portfolio securities are valued by reference to the fund's acquisition cost as adjusted for amortization of premium or accumulation of discount rather than by reference to their value based on current market factors.

(2) The "penny-rounding method pricing" is the method of computing an investment company's price per share for purposes of distribution, redemption and repurchase whereby the current net asset value per share is rounded to the nearest one percent.

(3) A "liquidity put" is a right to sell a specified underlying security or securities within a specified period of time and at a specified exercise price, that may be sold, transferred or assigned only with the underlying security or securities, and includes:

(i) A standby commitment that entitles the holder to achieve same day settlement and to receive an exercise price equal to the amortized cost of the underlying security or securities plus accrued interest, if any, at the time of exercise; and

(ii) A demand feature that entitles the holder to receive the principal amount of the underlying security or securities plus accrued interest, if any, at the time of exercise, and which may be exercised either (A) at any time, upon no more than seven days' notice; or (B) at specified intervals not exceeding one year and upon no more than seven days's notice.

(4) A variable rate instrument is one whose terms provide for the adjustment of its interest rate on set dates and which, upon such adjustment, can reasonably be expected to have a market value that approximates its par value.

(5) A floating rate instrument is one whose terms provide for the adjustment of its interest rate whenever a specified interest rate changes and which, at any time, can reasonably be expected to have a market value that approximates its par value.

(6) The term unaffiliated nationally recognized statistical rating organization shall mean any nationally recognized statistical rating organization, as that term is used in rule 15c3-1(c)(2)(vi)(F) under the Securities Exchange Act of 1934 [17 CFR 240.15c3-1(c)(2)(vi)(F)], that is not an affiliated person of the issuer of, or any insurer, guarantor or provider of credit support for, the instrument which the money market fund is considering acquiring.

(7) "One year" shall mean 365 days except, in the case of an instrument that was originally issued as a one year instrument, but had up to 375 days until maturity, one year shall mean 375 days.

3. By adding § 270.2a41-1 to read as follows:

§ 270.2a41-1 Valuation of standby commitments by registered investment companies.

A standby commitment as described in rule 2a-7(c)(3)(i) under the Act [17 CFR 270.2a-7(c)(3)(i)] may be assigned a fair value of zero, *Provided*, That:

(a) The standby commitment is not used to affect the company's valuation of the security or securities underlying the standby commitment; and

(b) Any consideration paid by the company for the standby commitment, whether paid in cash or by paying a premium for the underlying security or securities, is accounted for by the company as unrealized depreciation.

4. By amending § 270.12d3-1 by adding new paragraph (d)(8)(v) to read as follows:

§ 270.12d3-1 Exemption of acquisitions of securities issued by persons engaged in securities related businesses.

* * * * *

(d) * * *

(8) * * *

(v) Acquistion of liquidity puts, as defined in rule 2a-7 under the act (17

CFR 270.2a–7] in compliance with the provisions of that rule.

* * * * *

Regulatory Flexibility Certification

Pursuant to section 605(b) of the Regulatory Flexibility Act (15 U.S.C. 605(b), the Chairman of the Commission has certified that the proposed amendments to rules 2a–7 and 12d3–1 and proposed rule 2a4–1 will not, if adopted, have a significant impact on a substantial number of small entities. This certification, including the reasons therefor, is attached to this release.

Dated: July 1, 1985.

By the Commission.

John Wheeler,

Secretary.

Regulatory Flexibility Certification

I, John S.R. Shad, Chairman of the Securities and Exchange Commission, hereby certify pursuant to 5 U.S.C. 605(b) that the proposed amendments to rules 2a–7 (17 CFR 270.2a–7) and 12d3–1 (17 CFR 270.12d3–1), and proposed rule 2a41–1 under the Investment Company Act of 1940 ("Act") (15 U.S.C. 80a–1, et. seq.), set forth in Investment Company Act Release No. 14607, if promulgated, will not have a significant economic impact on a substantial number of small entities. The reason for this certification is that the proposed amendments to rule 2a–7 would simply allow certain open-end investment companies, known as "money market funds" to acquire put options for the purpose of enhancing the liquidity of their portfolio securities, and would define the circumstances under which such put options could affect the maturity of those securities. While the primary effect of these amendments would be to expand the class of securities in which municipal money market funds could invest, it does not appear that the economic impact of the amendments upon small entities would be significant. The proposed amendments would also redefine the role of the board of directors required by rule 2a–7, thereby clarifying the extent to which such determinations may be delegated to the management of such companies, and incorporating present industry practices into the text of the rule. This change would not appear to have any significant economic impact. The proposed amendments to rule 2a–7 would also allow money market funds to acquire portfolio securities in reliance on a high quality rating only if the rating is assigned by a nationally recognized statistical rating organization that is unaffiliated with the issuer of, or any insurer, guarantor or provider of credit support for the rated securities. It does not appear that any funds that are small entities are purchasing securities in reliance upon ratings that would not qualify under the proposed amendments. Proposed rule 2a41–1 and the proposed amendment to rule 12d3–1 would codify certain prior exemptive orders allowing investment companies to acquire a type of put option known as standby commitments and to assign a fair value of zero to such commitments. While the proposed rule and rule amendments would make it unnecessary for municipal funds to file applications for exemptive relief, it does not appear that a substantial number of small entities would be seeking such relief, since most of the funds seeking to acquire standby commitments and value them at zero have already applied for and received exemptive relief.

Dated: July 1, 1985.

John S.R. Shad,

Chairman.

[FR Doc. 85–16246 Filed 7–8–85; 8:45 am]

BILLING CODE 8010–01–M

DEPARTMENT OF TRANSPORTATION

Coast Guard

33 CFR Part 117

[CGD8–85–12]

Drawbridge Operation Regulation; Bayou Sara, AL

AGENCY: U.S. Coast Guard, DOT.

ACTION: Proposed rule.

SUMMARY: At the request of the Seaboard System Railroad, the Coast Guard is considering a change in the regulation governing the operation of the swing span railroad bridge over Bayou Sara, mile 0.1, near Saraland, Mobile County, Alabama, by requiring that at least eight hours advance notice be given for an opening of the draw from 6 p.m. to 10 .m. The bridge would open on signal outside these hours. Presently, the draw is required to open on signal from 6 a.m. to 10 p.m. and on four hours advance notice from 10 p.m. to 6 a.m., except that, during periods of severe storms or hurricanes the draw is required to open on signal. This proposal is being made because of infrequent requests to open the draw during the proposed advance notice period. This action should relieve the bridge owner of the burden of having a person available at the bridge between 6 p.m. and 10 a.m., and should still provide the reasonable needs of navigation.

DATE: Comments must be received on or before August 23, 1985.

ADDRESS: Comments should be mailed to Commander (obr), Eighth Coast Guard District, 500 Camp Street, New Orleans, Louisiana 70130. The comments and other materials referenced in this notice will be available for inspection and copying in Room 1115 at this address. Normal office hours are between 8:00 a.m. and 3:30 p.m., Monday through Friday, except holidays. Comments may also be hand-delivered to this address.

FOR FURTHER INFORMATION CONTACT: Perry Haynes, Chief, Bridge Administration Branch, at the address given above, telephone (504) 589–2965.

SUPPLEMENTARY INFORMATION: Interested persons are invited to participate in this proposed rulemaking by submitting views, comments, data or arguments. Persons submitting comments should include their names and addresses, identify the bridge, and give reasons for concurrence with or any recommended change in the proposal. Persons desiring acknowledgment that their comments have been received should enclose a stamped, self-addressed postcard or envelope.

The Commander, Eighth Coast Guard District, will evaluate all communications received and determine a course of final action on this proposal. This proposed regulation may be changed in the light of comments received.

Drafting Information

The drafters of this notice are Perry Haynes, project officer, and Steve Crawford, project attorney.

Discussion of Proposed Regulation

Vertical clearance of the bridge in the closed position is 3.0 feet above high water and 5.0 feet above low water. There are, on average, twelve (12) trains crossing the bridge daily. Navigation through the bridge consists of tugs with tows and pleasure boats. Data submitted by Seaboard System Railroad for the 12-month period from January 1984 through December 1984 show that this traffic through the bridge is as follows:

(1) During the proposed advance notice period of 6 p.m. to 10 a.m., there were 53 bridge openings—an average of 4.4 openings per month or an average of one opening every seven days.

(2) During the remaining hours between 10 a.m. and 6 p.m. when the draw would continue to open on signal, there were 134 bridge openings—an average of 11.2 openings per month or