FAA, Transport Airplane Directorate; or the Direction Générale de l'Aviation Civile (DGAC) (or its delegated agent).

Alternative Methods of Compliance

(c) An alternative method of compliance or adjustment of the compliance time that provides an acceptable level of safety may be used if approved by the Manager, International Branch, ANM–116. Operators shall submit their requests through an appropriate FAA Principal Maintenance Inspector, who may add comments and then send it to the Manager, International Branch, ANM–116.

Note 4: Information concerning the existence of approved alternative methods of compliance with this AD, if any, may be obtained from the International Branch, ANM–116.

Special Flight Permits

(d) Special flight permits may be issued in accordance with sections 21.197 and 21.199 of the Federal Aviation Regulations (14 CFR 21.197 and 21.199) to operate the airplane to a location where the requirements of this AD can be accomplished.

Incorporation by Reference

(e) Except as required by paragraph (b) of this AD: The actions shall be done in accordance with Airbus All Operators Telex A300–53A0361, dated June 14, 2001. This incorporation by reference was approved by the Director of the Federal Register in accordance with 5 U.S.C. 552(a) and 1 CFR part 51. Copies may be obtained from Airbus Industrie, 1 Rond Point Maurice Bellonte, 31707 Blagnac Cedex, France. Copies may be inspected at the FAA, Transport Airplane Directorate, 1601 Lind Avenue, SW., Renton, Washington; or at the Office of the Federal Register, 800 North Capitol Street, NW., suite 700, Washington, DC.

Note 5: The subject of this AD is addressed in French telegraphic airworthiness directive 2001–245(B), dated June 16, 2001.

Effective Date

(f) This amendment becomes effective on July 26, 2001.

Issued in Renton, Washington, on July 3, 2001.

Donald L. Riggin,

Acting Manager, Transport Airplane Directorate, Aircraft Certification Service.

[FR Doc. 01–17165 Filed 7–10–01; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 270 and 274

[Release No. IC–25058; File No. S7–21–99]

RIN 3235–AH56

Treatment of Repurchase Agreements and Refunded Securities as an Acquisition of the Underlying Securities

AGENCY: Securities and Exchange Commission.

ACTION: Final rule.

SUMMARY: The Securities and Exchange Commission is adopting a new rule and related rule amendments under the Investment Company Act of 1940 that affect the ability of investment companies to invest in repurchase agreements and pre-refunded bonds under the Act. The final rule codifies and updates staff positions that have permitted investment companies to ''look through'' counterparties to certain repurchase agreements and issuers of municipal bonds that have been ''refunded'' with U.S. government securities and treat the securities comprising the collateral as investments for certain purposes under the Act.

EFFECTIVE DATE: August 15, 2001.

FOR FURTHER INFORMATION CONTACT: Hugh Lutz, Attorney, or Martha B. Peterson, Special Counsel, Office of Regulatory Policy, at (202) 942–0690, Division of Investment Management, Securities and Exchange Commission, 450 5th Street, N.W., Washington, D.C. 20549–0506.

SUPPLEMENTARY INFORMATION: The Securities and Exchange Commission today is adopting new rule 5b–3 [17 CFR 270.5b–3] and conforming amendments to rules 2a–7 [17 CFR 270.2a–7] and 12d3–1 [17 CFR 270.12d3–1] under the Investment Company Act of 1940 [15 U.S.C. 80a] (''Investment Company Act'' or ''Act'').[1]

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Executive Summary

Repurchase agreements provide investment companies (''funds'') with a convenient means to invest excess cash on a secured basis, generally for short periods of time. In a typical fund repurchase agreement, a fund enters into a contract with a broker, dealer, or bank (the ''counterparty'' to the transaction) for the purchase of securities. The counterparty agrees to repurchase the securities at a specified future date, or on demand, for a price that is sufficient to return to the fund its original purchase price, plus an additional amount representing the return on the fund's investment.

The Commission is adopting rule 5b–3, which permits a fund, subject to certain conditions, to treat a repurchase agreement as an acquisition of the underlying collateral in determining whether it is in compliance with (i) the investment criteria for diversified funds set forth in section 5(b)(1) of the Act[2] and (ii) the prohibition on fund acquisition of an interest in a broker-dealer in section 12(d)(3) of the Act.[3] Rule 5b–3 also provides for similar ''look-through'' treatment for purposes of section 5(b)(1) of the Act in the case of an investment in state or municipal bonds, the payment of which has been fully funded by escrowed U.S. government securities.

The new rule codifies and updates staff interpretive and no-action letters. It is intended to adapt the Act to economic realities of repurchase agreements and pre-refunded bonds and reflects recent developments in bankruptcy law protecting parties to repurchase agreements.

[1] Unless otherwise noted, all references to rule 2a–7 or rule 12d3–1, or to any paragraph of those rules, will be to 17 CFR 270.2a–7 and 17 CFR 270.12d3–1, respectively.

[2] 15 U.S.C. 80a–5(b)(1).

[3] 15 U.S.C. 80a–12(d)(3).

I. Background

Repurchase agreements provide funds with a means to invest idle cash at competitive rates for short periods. While a repurchase agreement has legal characteristics of both a sale and a secured transaction, economically it functions as a loan from the fund to the counterparty, in which the securities purchased by the fund serve as collateral for the loan and are placed in the possession or under the control of the fund's custodian during the term of the agreement.[4]

Two provisions of the Act may affect a fund's ability to invest in repurchase agreements. Section 12(d)(3) of the Act generally prohibits a fund from acquiring an interest in a broker, dealer, or underwriter. Because a repurchase agreement may be considered to be the acquisition of an interest in the counterparty, section 12(d)(3) may limit a fund's ability to enter into repurchase agreements with many of the firms that act as counterparties.[5] Section 5(b)(1) of the Act limits the amount that a fund that holds itself out as being a diversified investment company may invest in the securities of any one issuer (other than the U.S. Government). This provision may limit the amount of repurchase agreements that a diversified fund may enter into with any one counterparty.

A fund investing in a properly structured repurchase agreement looks primarily to the value and liquidity of the collateral rather than the credit of the counterparty for satisfaction of the repurchase agreement. In two separate no-action positions issued in 1979 and 1980, the staff stated that, for purposes of sections 12(d)(3) and 5(b)(1) of the Act, a fund may treat a repurchase agreement as an acquisition of the underlying collateral if the repurchase agreement is ''collateralized fully.''[6] Because most repurchase agreements are collateralized fully by highly liquid U.S. government securities, this ''look-through'' treatment allowed funds to treat repurchase agreements as investments in government securities. As a result, a fund could invest in repurchase agreements with the same counterparty without the limitations of section 12(d)(3) or 5(b)(1).[7]

On September 23, 1999, the Commission issued a release proposing to codify and update these staff no-action positions.[8] We proposed new rule 5b–3 that would permit a fund, under certain circumstances, to look through repurchase agreements to the underlying securities for purposes of sections 5(b)(1) and 12(d)(3) of the Act. The proposed rule included conditions for looking through a repurchase agreement that were substantially similar to the conditions governing ''look-through'' treatment for money market funds under rule 2a–7 for purposes of complying with the rule's diversification requirements.[9] We also proposed to codify a 1993 staff no-action position that permits funds, under certain conditions, to look through pre-refunded bonds to the escrowed government securities for purposes of the section 5(b)(1) diversification requirements.[10] Finally, we proposed to eliminate a note to rule 12d3–1, which makes the rule's limited exemption from section 12(d)(3) of the Act unavailable for repurchase agreements, including those that were not collateralized fully.

The Commission received letters from four commenters on the Proposing Release, including the Investment Company Institute, which supported adoption of the rule.[11] We are adopting rule 5b–3, amendments to rule 2a–7, and amendments to rule 12d3–1, with certain changes suggested by these commenters.

II. Discussion

A. Qualifying Repurchase Agreements

New rule 5b–3(a) allows funds to treat the acquisition of a repurchase agreement as an acquisition of the underlying securities for purposes of sections 5(b)(1) and 12(d)(3) of the Act if the obligation of the seller to repurchase the securities from the fund is ''collateralized fully.''[12] A repurchase agreement is ''collateralized fully'' if: (i) The value of the underlying securities (reduced by the costs that the fund reasonably could expect to incur if the counterparty defaults) is, and at all times remains, at least equal to the agreed resale price;[13] (ii) the fund has perfected its security interest in the collateral; (iii) the collateral is maintained in an account of the fund with its custodian or a third party that qualifies as a custodian under the Act;[14] (iv) the collateral for the repurchase agreement consists entirely of: (A) Cash items; (B) U.S. government securities; (C) securities that at the time the repurchase agreement is entered into are rated in the highest category by the

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[4] *See* Treatment of Repurchase Agreements and Refunded Securities as an Acquisition of the Underlying Securities, Investment Company Act Release No. 24050 (Sept. 23, 1999) [64 FR 52476 (Sept. 29, 1999)] (''Proposing Release''), at n.4 and accompanying text.

[5] With minor exceptions, section 12(d)(3) prohibits an 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, [or] is engaged in the business of underwriting.'' The staff has taken the position that fund repurchase agreements with banks that are engaged in a securities-related business, including dealing in government securities, may be subject to the prohibitions of section 12(d)(3). *See* Letter from Gerald Osheroff, Associate Director, Division of Investment Management, to Matthew Fink, General Counsel, Investment Company Institute (May 7, 1985).

[6] In 1979, the staff announced that it would not recommend enforcement action under section 12(d)(3) if the repurchase agreement was ''structured in a manner reasonably designed to collateralize fully the investment company loan.'' Investment Company Act Release No. 10666 (Apr.18, 1979) [44 FR 25128 (Apr. 27, 1979)] (''Release 10666''). The following year, the staff applied this no-action position to a fund's compliance with the diversification requirements of section 5(b)(1) of the Act. MoneyMart Assets, Inc., SEC No-Action Letter (Sept. 3, 1980).

[7] Repurchase agreements with broker-dealers affiliated with the fund would, of course, continue to raise serious questions under sections 17(a) and 17(d) of the Act [15 U.S.C. 80a–17(a), 15 U.S.C. 80a–17(d)]. *See* Release 10666, *supra* note 6, at n.24.

[8] *See* Proposing Release, *supra* note 4.

[9] In 1996, when the Commission amended rule 2a–7, we tied the availability of ''look-through'' treatment to the preferred treatment given to repurchase agreements under the Bankruptcy Code and related insolvency statutes. *See* Revisions to Rules Regulating Money Market Funds, Investment Company Act Release No. 21837 (Mar. 21, 1996) [61 FR 13956 (Mar. 28, 1996)]. Proposed rule 5b–3 included similar requirements. In addition, we proposed conforming amendments to rule 2a–7 so that it would be consistent with rule 5b–3.

[10] T. Rowe Price Tax-Free Funds, SEC No-Action Letter (June 24, 1993). In the letter, the Division of Investment Management agreed not to recommend any enforcement action if a fund treated an investment in municipal bonds refunded with escrowed government securities as an investment in the government securities for purposes of section 5(b)(1). This no-action position was based on certain representations, including that (1) the deposit of the government securities was irrevocable and pledged only to the debt service on the original bonds, (2) payments from the escrow would not be subject to the preference provisions or automatic stay provisions of the Bankruptcy Code, and (3) no fund would invest more than 25 percent of its assets in the pre-refunded bonds of any single municipal issuer.

[11] The commenters included two trade associations, one investment adviser, and a bank. The comment letters are available in the Commission's Public Reference Room, 450 5th Street, N.W., Washington, D.C. (File No. S7–21–99).

[12] Rule 5b–3(a). A fund may only look through only that portion of the repurchase agreement that is collateralized fully. Any agreement or portion of an agreement that is not collateralized fully would be treated as a loan by the fund to the counterparty. Use of rule 5b–3(a) is optional: even if a fund can look through the repurchase agreement, it may choose to look to the counterparty rather than the underlying securities in meeting the diversification requirements of section 5(b)(1).

[13] The term ''resale price'' is defined in rule 5b–3(c)(7) as the acquisition price paid to the seller plus the accrued resale premium, *i.e.,* the return on investment specified in the agreement.

[14] We have revised this element of the rule to clarify that the collateral would have to be held by a custodian, or third party, in an account of the fund.

''Requisite NRSROs';[15] or (D) unrated securities that are of comparable quality to securities that are rated in the highest rating category by the Requisite NRSROs, as determined by the fund's board of directors or its delegate; and (v) the repurchase agreement qualifies for an exclusion from any automatic stay of creditors' rights against the counterparty under applicable insolvency law in the event of the counterparty's insolvency.

1. Acceptable Types of Collateral

New rule 5b–3 specifies the types of collateral that may be used to ''collateralize fully'' a repurchase agreement eligible for ''look-through'' treatment under the rule. We have expanded acceptable collateral to include unrated securities that are of comparable quality to securities that are rated in the highest rating category by the Requisite NRSROs, as determined by the investment company's board of directors or its delegate.[16] We are not, however, adopting a recommendation by two commenters that we altogether eliminate the rule's requirements regarding the credit quality of the collateral. A requirement that the underlying collateral be of highest quality limits a fund's exposure to the ability of the counterparty to maintain sufficient collateral. As we noted in the Proposing Release, securities of lower quality may be subject to greater price fluctuation. In the event of a steep drop in the market value of the collateral, the counterparty would have to deliver additional securities sufficient to ensure that the repurchase agreement remains fully collateralized. If the counterparty does not deliver sufficient additional securities and thus defaults, the fund may be unable to realize the full value of the repurchase agreement upon liquidation of the collateral. In addition, high quality securities are more readily liquidated than lower quality securities, in the event of a counterparty default.

2. Bankruptcy Treatment

Rule 5b–3 extends ''look-through'' treatment only to repurchase agreements that qualify for an exclusion from any automatic stay of creditors' rights under applicable bankruptcy laws.[17] Most comments supported this provision, which we are adopting as proposed. Failure of a repurchase agreement to qualify for an exclusion from an automatic stay would make ''look-through'' treatment inappropriate because the credit and liquidity risks assumed by the fund would be tied directly to the counterparty rather than the issuer of the underlying collateral.

3. Evaluating the Creditworthiness of Counterparties

We are eliminating the requirement, included in the staff no-action positions, and our proposal, that the fund's board of directors or its delegate evaluate the creditworthiness of the counterparty to a repurchase agreement. As one commenter observed, the creditworthiness assessment was required under the staff no-action letters because, at the time the letters were written, it was not clear whether a repurchase agreement would be subject to the automatic stay provision in the Bankruptcy Code, in the event that the counterparty became insolvent.[18] In light of subsequent amendments to the Code protecting the parties to repurchase agreements and our requirement that funds relying on the rule qualify for Bankruptcy Code protection,[19] we conclude that it is not necessary for the rule to contain a specific requirement that the fund's directors or their delegate assess the creditworthiness of the counterparty.[20]

B. Treatment of Pre-Refunded Bonds

We are adopting, as proposed, new rule 5b–3(b) which codifies, for purposes of section 5(b)(1), the conditions specified in the staff's no-action position permitting a fund to treat an investment in a ''refunded security'' as an investment in the escrowed U.S. government securities.[21] Under the rule, a ''refunded security'' is defined as a debt security the principal and interest payments of which are to be paid by U.S. government securities that have been irrevocably placed in an escrow account and are pledged only to the payment of the debt security.[22] The escrowed securities must not be redeemable prior to their final maturity, and the escrow agreement must prohibit the substitution of the escrowed securities unless the substituted securities are also U.S. government securities.[23] Finally, an independent certified public accountant must have certified to the escrow agent that the escrowed securities will satisfy all scheduled payments of principal, interest and applicable premiums on the refunded securities.[24] This treatment corresponds to the treatment that has been given to pre-refunded bonds in rule 2a–7.[25]

Commenters expressed support for the changes made by rule 5b–3(b), and we are adopting this provision as proposed.

C. Availability of Rule 12d3–1 for Repurchase Agreements

We are adopting, as proposed, an amendment to rule 12d3–1 that eliminates a note appended to the rule. Rule 12d3–1 provides limited exemptive relief from the prohibition in section 12(d)(3) of the Act against a fund acquiring an interest in a broker-dealer or a bank engaged in a securities-related business.[26] As discussed above, a fund

[15] The term ''Requisite NRSROs'' is defined in rule 5b–3(c)(6) as any two NRSROs, or, if only one NRSRO has issued a rating at the time the fund acquires the security, that NRSRO. ''NRSRO'' is defined in rule 5b–3(c)(5) as any nationally recognized statistical rating organization, as that term is used in paragraphs (c)(2)(vi)(E), (F) and (H) of rule 15c3–1 [17 CFR 240.15c3–1] under the Securities Exchange Act of 1934 [15 U.S.C. 78a–mm], that is not an ''affiliated person,'' as defined in section 2(a)(3)(C) of the Act [15 U.S.C. 80a–2(a)(3)(C)], of the issuer of, or any insurer or provider of credit support for, the security.

[16] Rule 5b–3(c)(1)(iv)(D).

[17] Rule 5b–3(c)(1)(v). *See* sections 101(47) of the Federal Bankruptcy Code (''Bankruptcy Code'') (defining ''repurchase agreement'') and 559 (protecting repurchase agreement participants from the Bankruptcy Code's automatic stay provisions). The Bankruptcy Code currently defines a repurchase agreement as:

An agreement, including related terms, which provides for the transfer of certificates of deposit, eligible bankers' acceptances, or securities that are direct obligations of, or that are fully guaranteed as to principal and interest by, the United States or any agency of the United States against the transfer of funds by the transferee of such certificates of deposit, eligible bankers' acceptances, or securities with a simultaneous agreement by such transferee to transfer to the transferor thereof certificates of deposit, eligible bankers' acceptances, or securities as described above, at a date certain no later than one year after such transfer or on demand, against the transfer of funds.

As a result, funds are limited in the collateral they can accept by both paragraph (c)(1)(iv)(D) of the rule and the provisions of the Bankruptcy Code (and other applicable insolvency laws) providing preferred treatment to qualifying repurchase agreements.

[18] *See* Proposing Release *supra* note 4 at nn.12–16 and accompanying text.

[19] Rule 5b–3(c)(1)(v).

[20] By omitting this requirement, we are not suggesting that it might not be prudent for an adviser to a fund to take precautions, including evaluating the creditworthiness of the counterparty, when entering into repurchase agreements on behalf of the fund.

[21] Rule 5b–3(b). Unlike the no-action position, the rule does not limit the amount of pre-refunded bonds of any one issuer that a fund can acquire. *See* T. Rowe Price Tax-Free Funds, *supra* note 10.

[22] Rule 5b–3(c)(4).

[23] Rule 5b–3(c)(4)(i), (ii).

[24] Rule 5b–3(c)(4)(iii). The rule makes an exception to the certification requirement if the refunded security has received the highest rating from an NRSRO. *Id.*

[25] *See* rule 2a–7(c)(4)(ii)(B). Technical amendments that we are adopting today will replace the definition of ''refunded security'' in rule 2a–7(a)(20) with a reference incorporating the definition that we are adopting in rule 5b–3(c)(4).

[26] Rule 12d3–1 provides an exemption for purchases of securities of any entity that derived fifteen percent or less of its gross revenues from securities related activities in its most recent fiscal year, unless the acquiring company would control the entity after the purchase. If the entity derived more than fifteen percent of its gross revenues from securities related activities, the rule provides a

that enters into a repurchase agreement with a broker-dealer or other counterparty that is engaged in securities related activities may be in violation of section 12(d)(3) of the Act, unless it is permitted to look through the agreement to the underlying collateral. The note appended to rule 12d3–1 has made the rule unavailable for repurchase agreements. With the elimination of this note, funds may rely on rule 12d3–1 even if the repurchase agreement does not meet the requirements for ''look-through'' treatment in rule 5b–3.[27]

D. Conforming Amendments to Rule 2a–7

We are also adopting conforming amendments to rule 2a–7. These amendments replace the definitions of ''collateralized fully,'' ''event of insolvency,'' and ''refunded security,'' currently set forth in rule 2a–7, with cross-references to the corresponding definitions in rule 5b–3.[28]

III. Effective Date

The new rule and rule amendments will be effective August 15, 2001.[29]

IV. Cost-Benefit Analysis

The Commission is sensitive to the costs and benefits imposed by its rules. For the most part, rule 5b–3 codifies current staff positions, and therefore will result in few marginal costs or benefits.[30] By codifying a number of staff no-action positions issued over a nearly twenty year period, the rule will give greater transparency to the Commission's rules in this area. In addition, the rule uses standards that are similar to those currently specified in rule 2a–7 for the treatment of repurchase agreements and pre-refunded bonds by money market funds. With this similar treatment, fund complexes that include money market funds may be more efficient in monitoring compliance with the requirements of the rules for all types of funds.

The rule is more restrictive than current requirements in two respects. First, as discussed above, rule 5b–3 is limited to repurchase agreements in which the underlying collateral consists of cash items, U.S. government securities, securities that are rated in the highest rating category by the Requisite NRSROs and unrated securities that are of comparable quality to securities that are rated in the highest rating category by the Requisite NRSROs, as determined by an investment company's board of directors or its delegate. This requirement is intended to ensure that the market value of the collateral will remain fairly stable and that the fund will be able to liquidate the collateral quickly in the event of a default. This limitation on collateral is more restrictive than the staff's position with respect to the treatment of repurchase agreements for purposes of section 12(d)(3),[31] but less restrictive than the staff's position with respect to section 5(b)(1).[32] Since most repurchase agreements are collateralized by U.S. government securities, which clearly fall within the rule's limitations, it appears that the limitation will not have any significant impact on funds.

Second, the rule is limited to repurchase agreements that qualify for an exclusion from any automatic stay under applicable insolvency law. Although this requirement is included in rule 2a–7, it was not a feature of the staff positions, which generally pre-dated the relevant changes in the Bankruptcy Code. Again, because most repurchase agreements qualify for an exclusion, this limitation should not have any significant impact on funds. The limitation will, however, provide important protections for investors by ensuring that a fund can liquidate the collateral quickly in the event of the counterparty's bankruptcy.

The use of rule 5b–3 is optional: even if a fund can look through a repurchase agreement, it may choose to look to the counterparty rather than the underlying securities in meeting the diversification requirements in section 5(b)(1). Thus, a fund may choose not to use rule 5b–3 if it determines that the costs of complying with the rule's requirements outweigh the benefits of being able to look through the repurchase agreement to the underlying securities.

The amendment to rule 12d3–1 eliminates the ''Note'' to the rule that renders the rule unavailable for repurchase agreements. This amendment will provide additional flexibility for funds without impairing investor protection.

V. Effects on Efficiency, Competition, and Capital Formation

Section 2(c) of the Investment Company Act requires the Commission, when engaging in rulemaking that requires it to consider or determine whether an action is consistent with the public interest, to consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.[33] Rule 5b–3 and the amendments to rules 2a–7 and 12d–3 are being adopted pursuant to the authority in section 6(c) and 38(a) of the Act.[34] Section 6(c) conditions rulemaking authority on the requirement that the rule be ''necessary or appropriate in the public interest''; therefore, the requirements of section 2(c) apply to rule 5b–3 and the rule amendments.

The Commission has considered whether this rulemaking will promote efficiency, competition, and capital formation. The rule and rule amendments generally codify the requirements for looking through repurchase agreements and pre-refunded bonds to the underlying securities for purposes of complying with sections 5(b)(1) and 12(d)(3) of the Act. Consistent with staff no-action positions, funds have been looking through repurchase agreements and pre-refunded bonds for a number of years. The few changes made by the rule and rule amendments generally are intended to reflect recent developments in bankruptcy law protecting parties to repurchase agreements and to adapt the Act to economic realities of repurchase agreements and pre-refunded bonds. These changes should not have a significant impact on funds. In addition,

limited exemption based on the amount and value of the securities purchased. The note to the rule stated: ''NOTE: It is not intended that this rule should supersede the requirements prescribed in Investment Company Act Release No. 13005 (Feb. 2, 1983) with respect to repurchase agreements with brokers or dealers.''

[27] By eliminating this note, we do not intend in any way to alter an adviser's duty of care with respect to the advice it provides a mutual fund, including the advice to enter into a repurchase agreement.

[28] Rule 2a–7(a)(5), (11), and (20) (cross-referencing rule 5b–3(c)(1), (2), and (4)). Rule 5b–3(c)(1) expands the types of collateral that may be used to collateralize fully a repurchase agreement to include certain high-quality, unrated securities. *See supra* note 16 and accompanying text. This expansion of acceptable collateral also applies to rule 2a–7.

[29] As we indicated in the Proposing Release, we are withdrawing all prior Commission and staff no-action and interpretive positions that are inconsistent with rule 5b–3. This withdrawal is effective [60 days after publication of the release in the **Federal Register**]. After this date, funds may ''look through'' repurchase agreements and pre-refunded bonds to the underlying collateral, for purposes of the Act, only if all of the requirements of rule 5b–3 are met.

[30] We received no response to the request for comment on the preliminary cost-benefit analysis that was included in the Proposing Release.

[31] Investment Company Act Release No. 13005 (Feb. 2, 1983) [48 FR 5894 (Feb. 9, 1983)] did not specify the type of collateral, merely noting that the ''securities most frequently used in connection with repurchase agreements are Treasury bills and other United States Government securities.''

[32] The staff's no-action position in MoneyMart Assets, *supra* note 6, was conditioned on the collateral consisting entirely of U.S. government securities.

[33] 15 U.S.C. 80a–2(c).

[34] 15 U.S.C. 80a–6(c) and 80a–38(a).

since the use of rule 5b–3 is optional, funds may choose to look to the repurchase agreement counterparty rather than the underlying securities in meeting the diversification requirements in section 5(b)(1). Given these factors, we believe that the rule and rule amendments will have no significant impact on efficiency, competition, and capital formation.

VI. Summary of Final Regulatory Flexibility Analysis

The Commission has prepared a Final Regulatory Flexibility Analysis (''FRFA'') in accordance with 5 U.S.C. 604 regarding rule 5b–3, and the amendments to rules 2a–7 and 12d3–1. A summary of the Initial Regulatory Flexibility Analysis (''IRFA''), which was prepared in accordance with 5 U.S.C. 603, was published in the Proposing Release. The following is a summary of the FRFA.

A. Need for and Objectives of the Rule Amendments

Rule 5b–3 generally codifies the staff's position that a fund may look through a fully collateralized repurchase agreement to the underlying securities for purposes of sections 5(b)(1) and 12(d)(3) of the Act. The rule also permits a fund to treat the acquisition of certain pre-refunded bonds as an acquisition of the escrowed securities for purposes of section 5(b)(1) of the Act. In addition, the amendment to rule 12d3–1 eliminates the ''Note'' appended to the rule in order to allow funds to rely on rule 12d3–1 even if the repurchase agreement is not collateralized fully. Finally, the amendments to rule 2a–7 are intended to simplify and update the provisions of that rule that address repurchase agreements and refunded securities.

B. Significant Issues Raised by Public Comments

The Commission received no comments on the IRFA.

C. Small Entities Subject to the Rules

For purposes of the Investment Company Act and the Regulatory Flexibility Act, a fund is a small entity if the fund, together with other funds in the same group of related funds, has net assets of $50 million or less as of the end of its most recent fiscal year.[35]

Rule 5b–3 and the amendment to rule 12d3–1 will affect any fund that invests in a repurchase agreement with a broker, dealer, underwriter, or bank that is engaged in a securities-related business, when the investment may otherwise be prohibited by section 12(d)(3) of the Act. In addition, rule 5b–3 will affect any fund that holds itself out as a diversified investment company under section 5(b)(1) of the Act and that invests in repurchase agreements or pre-refunded bonds.

As of December 31, 2000, there were approximately 4,145 registered funds that were not money market funds. The Commission staff estimates that 196 of these funds are small entities. We assume that all funds enter into repurchase agreements, and that many of these agreements are with broker-dealers or other counterparties that are engaged in a securities-related business. Therefore, we anticipate that all of the estimated 196 small entities will be affected by the rule's treatment of investments in repurchase agreements for purposes of section 5(b)(1) and 12(d)(3) of the Act, and the amendment to rule 12d3–1.

The FRFA explains that rule 5b–3 should not have a significant economic impact on these funds. The rule would not effect significant changes to the current treatment of repurchase agreements and pre-refunded bonds, but instead would generally codify and update a number of no-action positions that have been taken by the Commission staff. In addition, the amendment to rule 12d3–1 would benefit these funds by allowing them to rely on the rule even if the repurchase agreement does not meet the requirements for ''look-through'' treatment.

The amendments to rule 2a–7 affect money market funds. As of December 31, 2000, there were approximately 300 registered funds with one or more portfolios that are money market funds. The Commission staff estimates that approximately six of these funds are small entities. The amendments replace the definitions of ''collateralized fully,'' ''event of insolvency,'' and ''refunded security'' in rule 2a–7 with cross-references to the corresponding definitions in rule 5b–3. The cross-reference to the definition of ''collateralized fully'' in rule 5b–3 will allow money market funds to use unrated securities that are of comparable quality to securities that are rated in the highest rating category by the Requisite NRSROs to collateralize fully their repurchase agreements. This change will not have a significant impact on small entities because most repurchase agreements are collateralized fully by U.S. government securities. In addition, the cross-references to the definitions of ''event of insolvency'' and ''refunded security'' in rule 5b–3 will not have a significant impact on small entities because the cross-references do not involve any change in substantive requirements.

D. Projected Reporting, Recordkeeping, and Other Compliance Requirements

Rule 5b–3 and the amendments to rule 2a–7 and 12d–3 will not impose any new reporting or recordkeeping requirements. These provisions do not involve major changes in compliance requirements because they mainly codify existing Commission staff positions. There are no rules that duplicate, overlap or conflict with the rule and rule amendments.

E. Agency Action to Minimize Effects on Small Entities

The Regulatory Flexibility Act directs the Commission to consider significant alternatives that would accomplish the stated objective, while minimizing any significant economic impact on small entities. In connection with rule 5b–3 and the rule amendments, the Commission considered the following alternatives: (i) The establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities; (ii) the clarification, consolidation, or simplification of compliance and reporting requirements under the rule for small entities; (iii) the use of performance rather than design standards; and (iv) an exemption from coverage of the rule, or any part thereof, for small entities. The FRFA notes that rule 5b–3 and the rule amendments are not intended to effect major substantive changes to the current treatment of repurchase agreements and pre-refunded bonds, but would essentially codify a number of no-action positions taken by the Commission staff. Because rule 5b–3 and the rule amendments are designed to clarify the appropriate treatment of investments by funds in repurchase agreements and pre-refunded bonds for various purposes of the Act, and to provide investment flexibility for funds of all sizes, it would be inconsistent with the purposes of the Regulatory Flexibility Act to propose to exempt small entities from their coverage. Further clarification, consolidation, or simplification of the rules, or specification of different compliance standards for small entities, would not be appropriate, because the rules set forth the minimum standards consistent with investor protection. For the same reasons, the use of performance standards would be inappropriate. Overall, rule 5b–3 and the rule amendments will not have an adverse effect on small entities.

The FRFA is available for public inspection in File No. S7–21–99, and a

[35] 17 CFR 270.0–10.

copy may be obtained by contacting Hugh Lutz, Attorney, at (202–942–0690), Office of Regulatory Policy, Securities and Exchange Commission, 450 5th Street, N.W., Washington, D.C. 20549–0506.

VII. Statutory Authority

The Commission is adopting new rule 5b–3, and amending rule 2a–7 and rule 12d3–1, pursuant to the authority set forth in sections 6(c) and 38(a) of the Act [15 U.S.C. 80a–6(c) and 80a–37(a)]. The Commission is amending Form N–SAR pursuant to authority set forth in sections 13, 15(d) and 23(a) of the Securities Exchange Act of 1934 [15 U.S.C. 78m, 78o(d), and 78w(a)] and sections 8, 30 and 38 of the Investment Company Act of 1940 [15 U.S.C. 80a–8, 80a–29 and 80a–37].

List of Subjects in 17 CFR Parts 270 and Part 274

Investment companies, Reporting and recordkeeping requirements, Securities.

Text of Rule and Form Amendments

For the reasons set out in the preamble, Title 17, Chapter II of the Code of Federal Regulations is amended as follows:

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

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

Authority: 15 U.S.C. 80a–1 *et seq.*, 80a–34(d), 80a–37, 80a–39, unless otherwise noted;

* * * * *

2. Section 270.2a–7 is amended by revising paragraphs (a)(5), (a)(11), and (a)(20) to read as follows:

§ 270.2a–7 Money market funds.

(a) Definitions.

* * * * *

(5) *Collateralized Fully* means ''Collateralized Fully'' as defined in § 270.5b–3(c)(1).

* * * * *

(11) *Event of Insolvency* means ''Event of Insolvency'' as defined in § 270.5b–3(c)(2).

* * * * *

(20) *Refunded Security* means ''Refunded Security'' as defined in § 270.5b–3(c)(4).

* * * * *

3. Section 270.5b–3 is added to read as follows:

§ 270.5b–3 Acquisition of repurchase agreement or refunded security treated as acquisition of underlying securities.

(a) *Repurchase Agreements.* For purposes of sections 5 and 12(d)(3) of the Act (15 U.S.C. 80a–5 and 80a–12(d)(3)), the acquisition of a repurchase agreement may be deemed to be an acquisition of the underlying securities, provided the obligation of the seller to repurchase the securities from the investment company is Collateralized Fully.

(b) *Refunded Securities.* For purposes of section 5 of the Act (15 U.S.C. 80a–5), the acquisition of a Refunded Security is deemed to be an acquisition of the escrowed Government Securities.

(c) *Definitions.* As used in this section:

(1) *Collateralized Fully* in the case of a repurchase agreement means that:

(i) The value of the securities collateralizing the repurchase agreement (reduced by the transaction costs (including loss of interest) that the investment company reasonably could expect to incur if the seller defaults) is, and during the entire term of the repurchase agreement remains, at least equal to the Resale Price provided in the agreement;

(ii) The investment company has perfected its security interest in the collateral;

(iii) The collateral is maintained in an account of the investment company with its custodian or a third party that qualifies as a custodian under the Act;

(iv) The collateral consists entirely of:

(A) Cash items;

(B) Government Securities;

(C) Securities that at the time the repurchase agreement is entered into are rated in the highest rating category by the Requisite NRSROs; or

(D) Unrated Securities that are of comparable quality to securities that are rated in the highest rating category by the Requisite NRSROs, as determined by the investment company's board of directors or its delegate; and

(v) Upon an Event of Insolvency with respect to the seller, the repurchase agreement would qualify under a provision of applicable insolvency law providing an exclusion from any automatic stay of creditors' rights against the seller.

(2) *Event of Insolvency* means, with respect to a person:

(i) An admission of insolvency, the application by the person for the appointment of a trustee, receiver, rehabilitator, or similar officer for all or substantially all of its assets, a general assignment for the benefit of creditors, the filing by the person of a voluntary petition in bankruptcy or application for reorganization or an arrangement with creditors; or

(ii) The institution of similar proceedings by another person which proceedings are not contested by the person; or

(iii) The institution of similar proceedings by a government agency responsible for regulating the activities of the person, whether or not contested by the person.

(3) *Government Security* means any ''Government Security'' as defined in section 2(a)(16) of the Act (15 U.S.C. 80a–2(a)(16)).

(4) *Refunded Security* means a debt security the principal and interest payments of which are to be paid by Government Securities (''deposited securities'') that have been irrevocably placed in an escrow account pursuant to an agreement between the issuer of the debt security and an escrow agent that is not an ''affiliated person,'' as defined in section 2(a)(3)(C) of the Act (15 U.S.C. 80a–2(a)(3)(C)), of the issuer of the debt security, and, in accordance with such escrow agreement, are pledged only to the payment of the debt security and, to the extent that excess proceeds are available after all payments of principal, interest, and applicable premiums on the Refunded Securities, the expenses of the escrow agent and, thereafter, to the issuer or another party; *provided* that:

(i) The deposited securities are not redeemable prior to their final maturity;

(ii) The escrow agreement prohibits the substitution of the deposited securities unless the substituted securities are Government Securities; and

(iii) At the time the deposited securities are placed in the escrow account, or at the time a substitution of the deposited securities is made, an independent certified public accountant has certified to the escrow agent that the deposited securities will satisfy all scheduled payments of principal, interest and applicable premiums on the Refunded Securities; *provided, however,* an independent public accountant need not have provided the certification described in this paragraph (c)(4)(iii) if the security, as a Refunded Security, has received a rating from an NRSRO in the highest category for debt obligations (within which there may be sub-categories or gradations indicating relative standing).

(5) *NRSRO* means any nationally recognized statistical rating organization, as that term is used in paragraphs (c)(2)(vi)(E), (F) and (H) of § 240.15c3–1 of this chapter, that is not an ''affiliated person,'' as defined in section 2(a)(3)(C) of the Act (15 U.S.C.

80a–2(a)(3)(C)), of the issuer of, or any insurer or provider of credit support for, the security.

(6) *Requisite NRSROs* means:

(i) Any two NRSROs that have issued a rating with respect to a security or class of debt obligations of an issuer; or

(ii) If only one NRSRO has issued a rating with respect to such security or class of debt obligations of an issuer at the time the investment company acquires the security, that NRSRO.

(7) *Resale Price* means the acquisition price paid to the seller of the securities plus the accrued resale premium on such acquisition price. The accrued resale premium is the amount specified in the repurchase agreement or the daily amortization of the difference between the acquisition price and the resale price specified in the repurchase agreement.

(8) *Unrated Securities* means securities that have not received a rating from the Requisite NRSROs.

4. Section 270.12d3–1 is amended by removing the note following paragraph (d)(8).

PART 274—FORMS PRESCRIBED UNDER THE INVESTMENT COMPANY ACT OF 1940

5. The authority citation for Part 274 continues to read as follows:

Authority: 15 U.S.C. 77f, 77g, 77h, 77j, 77s, 78c(b), 781, 78m, 78n, 78o(d), 80a–8, 80a–24, and 80a–29, unless otherwise noted.

Note: The text of Form N–SAR does not, and this amendment will not, appear in the *Code of Federal Regulations*.

6. Form N–SAR (referenced in 17 CFR 274.101) is amended by revising the second sentence in the first paragraph of the Instructions to Specific Items 24 and 25 to read as follows:

FORM N–SAR

* * * * *

Instructions to Specific Items

* * * * *

ITEMS 24 and 25: Acquisition of securities of registrant's regular brokers or dealers

* * * *See* Rule 12d3–1, Investment Company Act Release No. 14036, dated July 13, 1984, adopting Rule 12d3–1, and Investment Company Act Release No. 25058, dated July 5, 2001, amending Rule 12d3–1. * * *

* * * * *

Dated: July 5, 2001.

By the Commission.

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 01–17302 Filed 7–10–01; 8:45 am]

BILLING CODE 8010–01–P

DEPARTMENT OF HEALTH AND HUMAN SERVICES

Food and Drug Administration

21 CFR Parts 510 and 558

Animal Drugs, Feeds, and Related Products; Tylosin; Withdrawal of Approval of NADAs

AGENCY: Food and Drug Administration, HHS.

ACTION: Final rule.

SUMMARY: The Food and Drug Administration (FDA) is amending the animal drug regulations to remove those portions that reflect approval of two new animal drug applications (NADAs) listed below. In a notice published elsewhere in this issue of the **Federal Register**, FDA is withdrawing approval of the NADAs.

DATES: This rule is effective July 23, 2001.

FOR FURTHER INFORMATION CONTACT: Pamela K. Esposito, Center for Veterinary Medicine (HFV–210), Food and Drug Administration, 7500 Standish Pl., Rockville, MD 20855, 301–827–5593.

SUPPLEMENTARY INFORMATION: Heinold Feeds, Inc., P.O. Box 377, Kouts, IN 46347, has requested that FDA withdraw approval of NADA 95–628 for Tylosin® Antibiotic Premix and NADA 127–506 for Tylan® Sulfa-G Premixes because the products are no longer manufactured or marketed.

Following the withdrawal of approval of these NADAs, Heinold Feeds, Inc., is no longer the sponsor of any approved applications. Therefore, 21 CFR 510.600(c) is amended to remove entries for this sponsor.

As provided below, the animal drug regulations are amended to reflect the withdrawal of approvals.

This rule does not meet the definition of ''rule'' in 5 U.S.C. 804(3)(A) because it is a rule of ''particular applicability.'' Therefore, it is not subject to the congressional review requirements in 5 U.S.C. 801–808.

List of Subjects

21 CFR Part 510

Administrative practice and procedure, Animal drugs, Labeling, Reporting and recordkeeping requirements.

21 CFR Part 558

Animal drugs, Animal feeds.

Therefore, under the Federal Food, Drug and Cosmetic Act and under authority delegated to the Commissioner of Food and Drugs and redelegated to the Center for Veterinary Medicine, 21 CFR parts 510 and 558 are amended as follows:

PART 510—NEW ANIMAL DRUGS

1. The authority citation for 21 CFR part 510 continues to read as follows:

Authority: 21 U.S.C. 321, 331, 351, 352, 353, 360b, 371, 379e.

§ 510.600 [Amended]

2. Section 510.600 *Names, addresses, and drug labeler codes of sponsors of approved applications* is amended in the table in paragraph (c)(1) by removing the entry for ''Heinold Feeds, Inc.,'' and in the table in paragraph (c)(2) by removing the entry for ''043727''.

PART 558—NEW ANIMAL DRUGS FOR USE IN ANIMAL FEEDS

3. The authority citation for 21 CFR part 558 continues to read as follows:

Authority: 21 U.S.C. 360b, 371.

§ 558.625 [Amended]

4. Section 558.625 *Tylosin* is amended by removing and reserving paragraph (b)(9).

§ 558.630 [Amended]

5. Section 558.630 *Tylosin and sulfamethazine* is amended in paragraph (b)(10) by removing ''043727,''; and by removing ''and 051359, 053389'' and by adding in its place ''051359, and 053389''.

Dated: July 2, 2001.

Stephen F. Sundlof,

Director, Center for Veterinary Medicine.

[FR Doc. 01–17407 Filed 7–10–01; 8:45 am]

BILLING CODE 4160–01–S

DEPARTMENT OF TRANSPORTATION

Coast Guard

33 CFR Part 117

[CGD08–01–014]

Drawbridge Operating Regulation; Green River, Spottsville, Kentucky

AGENCY: Coast Guard, DOT.

ACTION: Notice of temporary deviation from drawbridge regulations.