

because the Funds may be deemed to be affiliated persons by reasons other than having a common investment adviser, common directors, and/or common officers. Applicants state that Banknorth N.A., an affiliated person of BIA, owns as a fiduciary and has the power to vote more than 5% (and more than 25%) of the outstanding voting securities of each of the Funds. Therefore, the Acquiring Fund may be deemed a Second-Tier Affiliate of each Acquired Fund.

3. Section 17(b) of the Act provides, in relevant part, that the Commission may exempt a transaction from the provisions of section 17(a) if evidence establishes that the terms of the proposed transaction, including the consideration to be paid or received, are reasonable and fair and do not involve overreaching on the part of any person concerned, and the proposed transaction is consistent with the policy of each registered investment company concerned and the general purposes of the Act.

4. Applicants request an order under section 17(b) of the Act exempting them from section 17(a) to the extent necessary to consummate each Reorganization. Applicants submit that the Reorganizations satisfy the conditions of section 17(b) of the Act. Applicants also state that the Board, including all of the Disinterested Trustees, has found the participation of the Funds in the Reorganizations to be in the best interests of each Fund and its shareholders and that such participation will not dilute the interests of existing shareholders of each Fund. Applicants also state that the Reorganizations will be effected on the basis of relative net asset value.

For the Commission, by the Division of Investment Management, under delegated authority.

Margaret H. McFarland,
Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Investment Company Act Release No. 25651; 812-12811]

Principal Bond Fund, Inc., et al.; Notice of Application

July 8, 2002.

AGENCY: Securities and Exchange Commission ("Commission").

ACTION: Notice of an application under section 17(b) of the Investment Company Act of 1940 (the "Act") for an exemption from section 17(a) of the Act.

SUMMARY OF APPLICATION: Applicants request an order to permit a registered open-end management investment company to acquire all of the assets and assume all of the liabilities of another registered open-end management investment company. Because of certain affiliations, applicants may not rely on rule 17a-8 under the Act.

APPLICANTS: Principal Bond Fund, Inc. (the "Bond Fund"), Principal High Yield Fund, Inc. (the "High Yield Fund"), and Principal Management Corporation (the "Adviser").

FILING DATES: The application was filed on April 18, 2002. Applicants have agreed to file an amendment during the notice period, the substance of which is reflected in this notice.

HEARING OR NOTIFICATION OF HEARING: An order granting the application will be issued unless the Commission orders a hearing. Interested persons may request a hearing by writing to the Commission's Secretary and serving applicants with a copy of the request, personally or by mail. Hearing requests should be received by the Commission by 5:30 p.m. on July 30, 2002, and should be accompanied by proof of service on the applicants, in the form of an affidavit, or, for lawyers, a certificate of service. Hearing requests should state the nature of the writer's interest, the reason for the request, and the issues contested. Persons who wish to be notified of a hearing may request notification by writing to the Commission's Secretary.

ADDRESSES: Secretary, Commission, 450 Fifth Street, NW, Washington, DC 20549-0609; Applicants, c/o The Principal Financial Group, 711 High Street, Des Moines, Iowa 50392-0200.

FOR FURTHER INFORMATION CONTACT: Bruce R. MacNeil, Senior Counsel, at (202) 942-0634, or Todd Kuehl, Branch Chief, at (202) 942-0564 (Division of Investment Management, Office of Investment Company Regulation).

SUPPLEMENTARY INFORMATION: The following is a summary of the application. The complete application may be obtained for a fee at the Commission's Public Reference Branch, 450 Fifth Street, NW, Washington, DC 20549-0102 (telephone (202) 942-8090).

Applicants' Representations:

1. The Bond Fund (the "Acquiring Fund") and the High Yield Fund (the "Acquired Fund," together with the Acquiring Fund, the "Funds") are Maryland corporations and are registered under the Act as open-end management investment companies. The Adviser serves as the investment adviser to each Fund and is registered

under the Investment Advisers Act of 1940. The Adviser is an indirect wholly-owned subsidiary of Principal Financial Group, Inc. ("Principal Financial"). Principal Life Insurance Company ("Principal Life") is also an indirect wholly-owned subsidiary of Principal Financial. Principal Life, for its own account, owns more than 5% of the outstanding voting securities of the Acquired Fund.

2. On March 11, 2002, the board of directors of each Fund (each a "Board," together, the "Boards"), including in each case all of the directors who are not "interested persons," as defined in section 2(a)(19) of the Act ("Independent Directors"), approved an Agreement and Plan of Reorganization (the "Plan"). Under the Plan, the Acquiring Fund will acquire all of the assets and assume all of the liabilities of the Acquired Fund in exchange for shares of the designated class of the Acquiring Fund (the "Reorganization"). The closing of the Reorganization ("Closing") is expected to occur on July 31, 2002, (the "Closing Date"). The shares of the Acquiring Fund exchanged will have an aggregate net asset value equal to the aggregate net asset value of the Acquired Fund's shares determined as of the close of regular trading on the New York Stock Exchange on the Closing Date. The value of assets of the Funds will be determined in accordance with the Acquiring Fund's then current prospectus and statement of additional information (whose valuation procedures are identical to the Acquired Fund's). As soon as practicable after the Closing, the Acquired Fund will distribute pro rata to its shareholders of record, determined as of the close of business on the Closing Date, its shares of the Acquiring Fund received at the Closing and will be liquidated.

3. Each Fund offers Class A and Class B shares. Class A shares are subject to a front-end sales charge, rule 12b-1 distribution fees, service fees, and in some cases, a contingent deferred sales charge ("CDSC") and Class B shares are subject to rule 12b-1 distribution fees, service fees and a CDSC. Applicants state that the rights and obligations of each class of the Acquiring Fund are identical to those of the corresponding share class of the Acquired Fund. Shareholders of each class of the Acquired Fund will receive shares of the corresponding class of the Acquiring Fund. No sales charges or other fees will be imposed in connection with the Reorganization. For purposes of calculating any CDSC on shares of the Acquiring Fund, shareholders of the Acquired Fund will be deemed to have held the shares of the Acquiring Fund

since the date the shareholders initially purchased the shares of the Acquired Fund.

4. The Boards, including all of the Independent Directors, determined that the Reorganization is in the best interests of each Fund and its shareholders and that the interests of shareholders would not be diluted as a result of the Reorganization. In determining whether to approve the Reorganization, the Boards considered various factors, including: (a) The terms and conditions of the Reorganization; (b) the comparative investment performance of the Funds; (c) the possible advantages to the Acquired Fund's shareholders of investing in a larger asset pool with a higher quality of securities; (d) the federal income tax consequences to the Acquired Fund's shareholders; (e) the possible benefits of a larger asset base to portfolio management of the Acquiring Fund; (f) the compatibility of investment objectives and policies of the Funds and any changes to the objectives and policies of the Acquired Fund that will result from the Reorganization; and (g) the tax-free nature of the Reorganization.

5. Applicants also state that the Boards determined that the investment objectives, restrictions and policies of the Funds, though not identical, are similar and the range of credit qualities in which the Acquiring Fund invests should offer the Acquired Fund's shareholders some degree of continuity in investment exposure to high yield bonds as well as potential for reduced risk. Although there is overlap in the range of securities in which the Funds may invest, Applicants state, however, that the Acquired Fund's assets that are not eligible investment for the Acquiring Fund will be liquidated prior to the Closing and the Acquired Fund and its shareholders will be responsible for any brokerage expenses and tax consequences resulting from this liquidation. The Adviser will bear all of the other costs associated with the Reorganization.

6. The Reorganization is subject to a number of conditions precedent, including that: (a) The Acquired Fund's shareholders will have approved the Reorganization; (b) the Funds will have received opinions of counsel that the Reorganization will be tax-free for the Funds and their shareholders; (c) applicants will have received from the Commission the exemptive relief requested by the application; (d) an N-14 registration statement relating to the Reorganization will have become effective with the Commission; and (e) the Acquired Fund will declare to

shareholders of record on or prior to the Closing Date a dividend, which together with all previous dividends will have the effect of distributing to shareholders all of its income and all net realized capital gains, if any, as of the Closing. The Plan may be terminated by mutual consent of each Board at any time prior to the Closing Date. No material changes will be made to the Plan without prior approval of the Commission.

7. A registration statement on Form N-14 relating to the Reorganization, containing a proxy statement/prospectus, was filed with the Commission and declared effective and was mailed to the Acquired Fund's shareholders on May 20, 2002. A special meeting of the Acquired Fund's shareholders was held on June 26, 2002, and the Reorganization was approved.

Applicants' Legal Analysis

1. Section 17(a) of the Act prohibits any affiliated person of a registered investment company, or any affiliated person of that person, acting as principal, from selling to or purchasing from the registered investment company any security or other property. Section 2(a)(3) of the Act defines an "affiliated person" of another person to include: (a) Any person directly or indirectly owning, controlling, or holding with power to vote 5% or more of the outstanding voting securities of the other person; (b) any person 5% or more of whose outstanding voting securities are directly or indirectly owned, controlled, or held with power to vote by the other person; (c) any person directly or indirectly controlling, controlled by, or under common control with the other person; and (d) if the other person is an investment company, any investment adviser of that company.

2. Rule 17a-8 under the Act exempts certain mergers, consolidations, and sales of substantially all of the assets of registered investment companies that are affiliated persons, or affiliated persons of an affiliated person, solely by reason of having a common investment adviser, common directors, and/or common officers, provided, that certain conditions are satisfied.

3. Applicants state that they may not rely on rule 17a-8 because the Funds may be deemed to be affiliated persons for reasons other than those set forth in the rule. Applicants state that Principal Financial and the Adviser may be deemed to control the Funds. Also, Principal Life owns more than 5% of the total outstanding voting securities of the Acquired Fund. The Acquired Fund, pursuant to section 2(a)(3)(B) of the Act, is an affiliated person of Principal Life and Principal Financial because

Principal Life has the power to vote more than 5% of the outstanding voting securities of the Acquired Fund. The Acquired Fund therefore may be an affiliated person of an affiliated person of the Acquiring Fund.

4. Section 17(b) of the Act provides, in relevant part, that the Commission may exempt a transaction from the provisions of section 17(a) if evidence establishes that the terms of the proposed transaction, including the consideration to be paid or received, are reasonable and fair and do not involve overreaching on the part of any person concerned, and the proposed transaction is consistent with the policy of each registered investment company concerned and the general purposes of the Act.

5. Applicants request an order under section 17(b) of the Act exempting them from section 17(a) to the extent necessary to effect the Reorganization. Applicants submit that the Reorganization satisfies the conditions of section 17(b) of the Act. Applicants also state that the Boards, including all of the Independent Directors, have determined that the participation of the Funds in the Reorganization is in the best interests of each Fund and that such participation will not dilute the interests of existing shareholders of each Fund. Applicants also state that the Reorganization will be effected on the basis of relative net asset value.

For the Commission, by the Division of Investment Management, under delegated authority.

Margaret H. McFarland,

Deputy Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-46166; File No. SR-DTC-2001-14]

Self-Regulatory Organizations; the Depository Trust Company; Order Approving a Proposed Rule Change Relating to the Closing of the Mortgage-Backed Securities Division of the Depository Trust Company

July 3, 2002.

On July 24, 2001, The Depository Trust Company ("DTC") filed with the Securities and Exchange Commission ("Commission") a proposed rule change pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"). Notice of the proposal was published in the **Federal Register** on