

Regional Headquarters Building, Federal Aviation Administration, 901 Locust, Kansas City, MO 64106; telephone (816) 329-2525.

#### SUPPLEMENTARY INFORMATION:

#### History

On September 2, 1999, the FAA published in the **Federal Register** a direct final rule; request for comments which revises the Class E airspace at Herington, KS (FR document 99-22890, 64 FR 48086, Airspace Docket No. 99-ACE-41). An error was subsequently discovered in the spelling of Herington. This action corrects that error. After careful review of all available information related to the subject presented above, the FAA has determined that air safety and the public interest require adoption of the rule. The FAA has determined that this correction will not change the meaning of the action nor add any additional burden on the public beyond that already published. This action corrects the error in the spelling of Herington and confirms the effective date to the direct final rule.

The FAA uses the direct final rulemaking procedure for a non-controversial rule where the FAA believes that there will be no adverse public comment. This direct final rule advised the public that no adverse comments were anticipated, and that unless a written adverse comment, or a written notice of intent to submit such an adverse comment, were received within the comment period, the regulation would become effective on December 30, 1999. No adverse comments were received, and thus this notice confirms that this direct final rule will become effective on that date.

#### Correction to the Direct Final Rule

Accordingly, pursuant to the authority delegated to me, the spelling of Herington, as published in the **Federal Register** on September 2, 1999 (64 FR 48086), (**Federal Register** Document 99-22890; page 48087, column three) is corrected as follows:

#### § 71.1 [Corrected]

ACE KS E5 Herington, KS [Corrected]

On page 48087, in the third column, correct the text header by removing Herington and substituting Herington.

On page 48087, in the third column, correct lines 2, 6 and 8 in the airspace designation by removing Herington and substituting Herington.

Issued in Kansas City, MO on November 18, 1999.

**Richard L. Day,**

*Acting Manager, Air Traffic Division, Central Region.*

[FR Doc. 99-31519 Filed 12-3-99; 8:45 am]

BILLING CODE 49103-13-M

## COMMODITY FUTURES TRADING COMMISSION

### 17 CFR Parts 3 and 32

RIN 3038-AB43

#### Trade Options on the Enumerated Agricultural Commodities

**AGENCY:** Commodity Futures Trading Commission.

**ACTION:** Final rulemaking.

**SUMMARY:** The Commodity Futures Trading Commission (Commission or CFTC) in April 1998, removed a long-standing prohibition on the offer and sale of off-exchange trade options on certain agricultural commodities subject to a number of regulatory requirements. On August 31, 1999, the Commission proposed to amend a number of those requirements. 64 FR 47452. The Commission is adopting as final those proposed amendments. In particular, the Commission is permitting cash settlement and offset or cancellation of agricultural trade options. It is also eliminating the transaction-specific disclosure statement, revising the summary disclosure statement provided to customers when opening an account and streamlining the registration requirements for Agricultural Trade Option Merchants (ATOMs) and their sales agents and certain reporting and recordkeeping requirements. The Commission believes that these amendments will increase the commercial utility of agricultural trade options while maintaining basic customer protections.

**EFFECTIVE DATE:** February 4, 2000.

**FOR FURTHER INFORMATION CONTACT:** Paul M. Architzel, Chief Counsel, Division of Economic Analysis, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW., Washington, DC 20581, (202) 418-5260, or electronically at [Parchitzel@cftc.gov].

#### SUPPLEMENTARY INFORMATION:

##### I. Background

In April 1998, the Commission promulgated interim final rules to permit the trading of agricultural trade options subject to various regulatory

requirements.<sup>1</sup> 63 FR 18821 (April 16, 1998). These requirements provided a number of customer protections, including limitations on the types of instruments or strategies permitted to be traded, registration of ATOMs, disclosure of risks to option buyers, financial safeguards, and recordkeeping. No one has applied for registration as an ATOM since the interim rules became effective in June 1998. Some observers have suggested that certain of the interim final rules' provisions discourage participation, and agricultural trade options would be offered more readily if the rules were modified.<sup>2</sup>

#### A. Proposed Revisions to the Agricultural Trade Option Rules

Based in part on those views, the Commission published a notice of proposed rulemaking (proposed rulemaking) reconsidering a number of the requirements of the agricultural trade option rules "with a view toward maintaining their basic customer protection while increasing the

<sup>1</sup> Generally, the offer or sale of commodity options is prohibited except on designated contract markets. 17 CFR 32.11. One of several specified exceptions to the general prohibition on off-exchange options is for "trade options." "Trade options" are off-exchange options "offered by a person having a reasonable basis to believe that the option is offered to" a person or entity within the categories of commercial users specified in the rule, where such commercial user "is offered or enters into the commodity option transaction solely for purposes related to its business as such." 17 CFR 32.4(a). However, this exception from the general ban on off-exchange options does not apply to trade options on the agricultural commodities enumerated in the Commodity Exchange Act (Act), 7 U.S.C. 1a(3). A full statement of the statutory and regulatory history is provided in the notice of final rulemaking promulgating the interim final rules. 63 FR 18821 (April 16, 1998).

<sup>2</sup> The Commission receives the views of a cross-section of the agricultural sector through its Agricultural Advisory Committee (AAC). The AAC, at its meeting on April 21, 1999, engaged in a detailed discussion of various policy issues raised by possible rule alternatives. Subsequently, nine organizations representing a broad cross-section of production agriculture submitted to the Commission their common views on these issues by letter dated April 23, 1999. The nine producer organizations were: (1) American Farm Bureau Federation, (2) National Association of Wheat Growers, (3) National Corn Growers Association, (4) National Farmers Union; (5) National Pork Producers, (6) American Soybean Association, (7) National Cattlemen's Beef Association, (8) National Cotton Council of America, and (9) National Grain Sorghum Producers.

Additional letters were submitted by the Farm Credit Council (dated April 19, 1999), the Illinois Farm Bureau (dated April 21, 1999), the National Grain and Feed Association (NGFA) (dated June 15, 1999), the Chicago Board of Trade (CBT) (dated June 16, 1999), the National Grain Sorghum Producers (dated July 9, 1999), and the American Farm Bureau Federation, the National Association of Wheat Growers, the American Soybean Association and the National Farmers Union (joint letter dated August 9, 1999).

commercial utility of the instruments or trading strategies permitted and streamlining regulatory or paperwork burdens." 64 FR 47452 (August 31, 1999). In particular, the Commission proposed to streamline the registration requirements for ATOMs and their sales agents by, among other things, removing the training requirement for associated persons and limiting the number of principals that must certify that they are not subject to statutory disqualification from registration. In addition, the Commission proposed to permit cash settlement and offset or cancellation of agricultural trade options by removing the requirement that such options, if exercised, must result in physical delivery. The Commission also proposed to eliminate the transaction-specific disclosure statement and to revise the summary disclosure statement provided to customers when opening an account. The Commission also proposed to streamline certain reporting and recordkeeping requirements. It also considered, but did not propose, permitting producers to write call options or changing the \$10 million exemptive level.

#### B. Comments

The Commission received a total of 22 comment letters, including those recommending that the Commission propose various amendments to the interim final rules. See note 2 *supra*. Overall, the comment letters expressed a wide range of opinions. Five commenters, including one academic, two introducing brokers (IBs), one commodity trading advisor (CTA)/IB and the National Introducing Brokers Association (NIBA) generally opposed the proposed changes. They expressed the view that the proposed amendments would weaken existing customer protections, increase the opportunity for fraud and abuse and facilitate poor business practices on the part of those offering or soliciting agricultural trade options.

Eight commenters, including four agribusinesses, three trade associations and one risk management firm, generally supported the proposed changes. They particularly supported the proposal to permit cash settlement and offset or cancellation of the option contracts, but argued that the Commission should go farther in easing the rule's requirements. They especially objected to the \$10 million dollar exemption level and to the requirement that option vendors and their sales agents be registered with the Commission. In contrast, the nine producer organizations strongly supported retaining the registration

requirement, including the associated right of a registrant's customers to bring grievances arising from a violation of the Act or Commission rules before the Commission's reparations forum, and opposed lowering the \$10 million exemption level.<sup>3</sup>

## II. The Final Rules

### A. Registration

As the Commission noted in its proposed rulemaking, "[t]he requirement that all market profession[als] be registered, and the authority to approve or revoke registrations, is an important means of policing conduct in a market." 64 FR 47453. As the Commission explained in the proposed rulemaking, with registration customers have available to them the Commission's reparations forum for dispute resolution.<sup>4</sup> Although there is "substantial support for a registration requirement, both because of the higher level of customer protection it provides and a desire to have available the Commission's reparations forum for dispute resolution," potential agricultural trade option vendors are opposed to the registration requirement. *Id.* Accordingly, the Commission specifically invited comments in the proposed rulemaking on the issue.

The NGFA's comment letter opposed a registration requirement and urged the Commission to "seriously consider notification as an alternative".<sup>5</sup> NGFA's continued opposition to registration flows from its opposition to the availability of Commission reparations proceedings to customers to resolve disputes with ATOMs involving trade options. NGFA voiced particular concern that the availability of reparations to resolve disputes involving trade options might expose

<sup>3</sup> Additional comments were submitted by the Chicago Board of Trade (CBT), the Chicago Mercantile Exchange (CME) and a futures commission merchant (FCM). The CBT concurred with many of the proposed changes, noting that it was "pleased that the Commission has incorporated several of [the CBT's] recommendations into [the Commission's] proposed rulemaking." See the CBT's comment letter at p. 1. The CME did not address the specific issues raised in the proposed rulemaking.

<sup>4</sup> Specifically:

[S]ection 14 of the Act provides that 'any person complaining of any violation of any provision of this Act or any rule \* \* \* issued pursuant to this Act by any person who is registered under this Act' may bring a reparations action [b]efore the Commission. Accordingly, complaints that do not relate to violations of the Act or Commission rules are not subject to Commission reparations proceedings.

*Id.*

<sup>5</sup> See the letter of September 30, 1999 from NGFA to the Commission.

ATOMs to reparations cases involving cash contracts.<sup>6</sup>

In contrast, the nine producer organizations expressed strong support for maintaining the registration requirement. Other commenters, including NIBA, an academic and other Commission registrants agreed. In general, these commenters were of the view that registration of those offering or soliciting agricultural trade options is an essential customer protection which should be mandatory.

Based upon thorough and careful consideration of the comments, the Commission has determined to retain the current registration requirement, which includes the statutory right to seek redress of violations of the Act or Commission rules through Commission reparations proceedings. This is particularly appropriate because although "some sectors of agriculture may have well-regarded industry arbitration fora available, many do not. For these sectors, reparations may be the only readily available non-judicial avenue for dispute resolution." 64 FR 47453.<sup>7</sup>

In retaining the registration requirement for ATOMs and their APs, the Commission notes that reparation proceedings are available only where a violation of the Act or Commission rules is alleged. Under the Commission's rules, the Director of the Office of Proceedings forwards a complaint and answer if the facts alleged so warrant. If no violation of the Act or Commission rules is alleged, the Director of the Office of Proceedings may terminate consideration of the filings. See, 17 CFR 12.26, 12.27. A dispute arising solely out of a cash market transaction, therefore, would be dismissed and not forwarded for adjudicatory action.

### 1. Simplification of the Registration Process

The Commission proposed a number of modifications based upon the acknowledged "broad agreement that the registration procedures for ATOMs and their sales agents be streamlined

<sup>6</sup> Other commenters, including three agribusinesses, concurred in NGFA's position. They noted that the reparations requirement might deter them, as well as others, from offering these instruments. One commenter, Consolidated Grain and Barge, Co., expressed particular support for the NGFA arbitration system. The CBT also supported rules permitting required dispute resolution under industry arbitration procedures such as the NGFA's trade rules.

<sup>7</sup> The Commission is also incorporating, as proposed, streamlined procedures clarifying the use of pre-dispute arbitration clauses for agricultural trade options and the procedures by which customers can waive their right to use Commission reparations procedures to resolve disputes with an ATOM.

and simple." Id. at 47454. Specifically, the Commission proposed removal of the requirement that ATOMs separately certify the truth of their principals' and APs' applications. The Commission also proposed to limit the principals required to file as part of an ATOM's application to those principals who exercise direct control over the ATOM's business affairs. In addition, the Commission proposed deletion of the mandatory six-hour training course for ATOMs' sales agents.

NIBA, the academic commenter and the registrants opposed the proposed amendments, particularly deletion of the mandatory six-hour training required of APs. NGFA, the agribusinesses, a trade association, and the CBT supported the proposed changes, although several opined that the proposed changes did not go far enough. The three agribusinesses particularly commended the Commission for proposing to delete the mandatory AP training requirement.

The Commission is adopting the proposed amendments to the registration procedures as final rules. In doing so, it has modified the definition of an AP, as provided in Commission Rule 3.13(a)(2)(ii), to include those who "supervise directly," an ATOMs' associated persons. The Commission also is modifying Rule 3.13(b) to state that those who "supervise directly" an ATOMs' associated persons, must register as an AP. These modifications clarify that only immediate supervisors of associated persons must register as APs (in addition to principals of the firm who control or direct the ATOM's activities) and must certify that they are not disqualified from registration under the Act. These modifications clarify that second or third tier supervisors are not covered by the registration and certification requirements.

In addition to the proposed amendments, the Commission requested comment on the relative burden and benefits of the current requirement that ATOMs notify the NFA when an associated person leaves its employ or when a new associated person begins. Generally, commenters did not respond to the request for comment. However, as some have observed, ATOMs, particularly those with a decentralized sales force, potentially will benefit from the requirement, which offers customers a means to determine whether an individual is duly authorized to offer and sell trade options on an ATOM's behalf. Accordingly, the Commission is retaining the requirement.<sup>8</sup>

<sup>8</sup> Under prior Commission Rule 3.13(c)(2), when an AP ceased to be associated with an ATOM, the

## 2. Commission Processing of Applications

Seven commenters addressed specifically the Commission's request for comments on the possible benefits to ATOMs, their APs or potential customers from the Commission's direct processing of registration applications, and the relative costs of such a proposal. Four commenters opined that it would be more efficient for NFA to perform this administrative task on the Commission's behalf as the interim final rules currently provide.<sup>9</sup> Two commenters disagreed, raising concerns regarding the degree of regulatory oversight NFA will have in performing this function.

The Commission remains convinced that NFA should perform these functions on the Commission's behalf. In reaching this conclusion, the Commission found that the possible benefits to ATOMs and their APs or potential customers from the Commission's direct processing of registration applications did not outweigh the relative costs of such a proposal.<sup>10</sup> Accordingly, the Commission finds it appropriate that NFA, which has the capacity to process registration applications with only minor changes to its existing systems, will perform these functions.<sup>11</sup>

Finally, one commenter suggested that the Commission permit potential

ATOM was required to notify NFA of that disassociation within 20 days of the disassociation's occurrence. The Commission has revised Rule 3.13(c)(2) to extend this notification time period to 45 days to enable smaller businesses to perform this notification as part of their routine month-end accounting.

<sup>9</sup> Under the interim final rules, the Commission delegated to NFA the authority to directly process applications for registration as an ATOM or an AP of an ATOM.

<sup>10</sup> As the Commission explained in the proposed rulemaking, during the 1980s, it:

[C]ompletely transferred [its registration administrative functions] to NFA \* \* \* and no longer has systems in place to process [registration applications such as those filed by ATOMs or their APs]. Accordingly, the Commission would have to rebuild this capability from the ground up before it could begin reviewing and approving registrations once again. Moreover, rebuilding such administrative systems would, in the short-run, compete for technical resources that are being devoted to Y2K compliance.

64 FR 47454.

<sup>11</sup> NGFA expressed that the Commission should clarify what degree of "regulatory authority" NFA will have in processing applications. In this regard, as explained by the Commission in its proposed rulemaking, these final rules, like the prior interim final rules, "strictly limit NFA's role. NFA does not become a self-regulatory authority for ATOMs simply by administratively processing their registration applications on the Commission's behalf. NFA exercises no regulatory authority over the offer or sale of agricultural trade options by ATOMs as a consequence of that administrative function, nor do ATOMs or their APs thereby become members of NFA." Id.

registrants to begin filing for registration with the NFA as ATOMs and their APs in reliance upon the amended registration conditions in advance of the effective date of the rules. The Commission will take no adverse action in connection with an ATOM and its APs processing or submitting registration materials with the NFA in reliance on these amended procedures in advance of the rule's effective date.<sup>12</sup> Because currently there are no registered ATOMs, to the extent that the amended rules increase the likelihood of registration and competition to be the first registered, an initial surge may cause administrative delay. This no-action position is in the public interest because it will enable ATOMs and their APs an initial period during which to process and submit their registrations with NFA so that all interested ATOMs may begin offering and selling trade options under the amended rules as soon as the rules become effective, in time for the coming crop year. This will provide producers with greater availability of instruments and choice in vendors in time to meet their hedging needs for the coming crop year.

## B. Cash Settlement

In proposing to permit cash settlement and offset or cancellation of agricultural trade options, the Commission noted its widespread support "among all sectors of agriculture." Id. at 47455. In addition, the Commission proposed to require ATOMs to provide customers with an account statement following the termination, cancellation, cash settlement or amendment of an option's expiration date (rolling the contract). In making this proposal, the Commission explained that:

[C]ustomers could have expected to have their accounts settled upon physical delivery, and this requirement will ensure that customers who cash settle their contracts are provided with similar information. Moreover, by receiving an accounting and knowing with certainty the outcome of their closed position, customers should better be able to ascertain the potential outcome of entering into a subsequent transaction.

Id.<sup>13</sup>

The majority of commenters strongly approved of the proposed change,

<sup>12</sup> Although ATOMs and their APs may have their registration applications processed in reliance upon the amended rules, unless they are registered in compliance with the current rules, they may not offer or sell these instruments until the rule amendments are effective.

<sup>13</sup> The Commission also noted that "[i]n addition, the Disclosure Statement continues to advise potential purchasers that trade options are required to have a business purpose and are not to be used for speculation." Id.

noting that it is "critical" to increasing the "effectiveness and flexibility of these products for both buyers and sellers."<sup>14</sup> A minority of commenters opposed the proposal, however, voicing concern that if cash settlement is permitted, agricultural trade options "could easily develop into an off-exchange traded speculative marketplace."

The Commission is adopting the rule as proposed, including the requirement that ATOMs provide customers with an account statement following the termination, cancellation, cash settlement or amendment of an option's expiration date (rolling the contract). The Commission is also clarifying that commercial enterprises eligible to be ATOMs include those selling inputs used in producing the commodity as well as banks that routinely finance businesses involved in the production, processing or handling of the commodity. 64 FR 47455.<sup>15</sup>

### C. Risk Disclosure, Customer Account Information and Reports to the Commission

#### 1. Risk Disclosure

The interim final rules required that customers be provided with both a general, summary disclosure statement upon opening an account and transaction-specific disclosures before entering into a specific transaction.<sup>16</sup> However, as noted by the Commission in the notice of proposed rulemaking, representatives of both potential trade option vendors and customers agreed that many of the transaction-specific disclosures could be made in the summary disclosure statement and others readily ascertainable from the face of the option contract itself, thus permitting the elimination of the transaction-specific disclosure requirement. *Id.* Accordingly, the Commission proposed to streamline risk disclosure by revising the summary

<sup>14</sup> See the CBT's letter of September 30, 1999 to the Commission.

<sup>15</sup> An FCM submitted a comment letter to the Commission requesting clarification on whether FCMs can register to become ATOMs. The Commission believes that an FCM may satisfy the requirements of Rule 32.13(a) and be allowed to become an ATOM. However, there are issues unique to FCMs, including possible procedures to address potential conflict of interest by a fiduciary's becoming the principal of an off-exchange transaction and the effect of that position on the FCM's required net capital. The Commission will consider these issues in a separate **Federal Register** release.

<sup>16</sup> The transaction-specific disclosure included information relating to the specific terms of a particular transaction. The ATOM was required to disclose the customer's worst possible financial outcome when the option premium was not collected up front or when an option contract was amended.

disclosure to include some of the material that formerly was included in the transaction-specific disclosure. *Id.*

Although two commenters supported retention of the current risk disclosure rules, a number of commenters described the proposed amendments as "positive."<sup>17</sup> The Commission is adopting the rules as proposed.

#### 2. Customer Account Information

In addition to proposing revisions to streamline the risk disclosure requirements, the Commission proposed to amend the requirements relating to reporting of account information to customers.<sup>18</sup> As explained in the proposed rulemaking:

A number of sources, including several state-level representatives of producers and commodity first handers, suggested that the requirements that ATOMs provide customers with account-related information potentially created too great a paperwork burden for smaller firms. \* \* \* Similarly, some have observed that oral contracting is still the prevailing means of transacting business in certain agricultural cash markets, and they suggest that the interim rules, which require agricultural trade option contracts to be written, should be amended to reflect that reality. In this regard, state law has recognized this practice by recognizing the validity of such oral contracts when they have been confirmed in writing.

64 FR 47455-47456.

One commenter opined that "verbal confirmation is not an acceptable business practice." The Commission agrees that best business practice is for all such communications to be in writing, including the option contract itself at the time the contract is made. However, there was consensus among representatives of potential vendors and purchasers that the Commission's rules should be amended to correspond more closely to current practice permitted under state law. Accordingly, the Commission is adopting the rule amendments as proposed, permitting ATOMs to enter into a contract orally, with subsequent written confirmation.<sup>19</sup> The written confirmation, which must

<sup>17</sup> Cargill, in its comment characterized them as "reasonable" and "necessary." See the letter of September 30, 1999 from Cargill Grain Division to the Commission.

<sup>18</sup> Specifically, under prior Rule 32.13(b), ATOMs were required to provide customers with written confirmation of contracts within 24 hours of executions and within 48 hours of a customer request, a written response regarding the customer's account or position. In addition, ATOMs were required to notify customers in writing of an option's expiration within the coming calendar month.

<sup>19</sup> The Commission notes that a customer retains the right to have a written agricultural trade option contract and that, unless the customer chooses to contract orally, the ATOM must provide the agricultural trade option contract to the customer in writing.

be signed by the ATOM, must include all material terms of the option contract. The rules further permit use of oral communications and notice to customers with respect to account information.

#### 3. Reports to the Commission

The interim rules required ATOMs to file reports on volume and open interest four times a year with the NFA. In response to this requirement, the Commission observed that there was "widespread support among agricultural groups for reducing ATOMs required reports." 64 FR 47456. In light of this, the Commission proposed to reduce periodic reporting to one annual report, filed by the ATOM with the Commission within 90 days of the end of its fiscal year.

Commenters addressing this specific proposed change offered a variety of views. One commenter, an agribusiness, disfavored having this reporting requirement, indicating that while the Commission was proceeding in the right direction by reducing the number of required reports, ultimately, it should delete the requirement all together. However, other commenters, including two agribusinesses and NGFA, voiced their support for this proposed amendment. In particular, one agribusiness stated that "the switch to annual reporting will greatly reduce the paperwork required to participate in the program."

Taking these comments into consideration, the Commission believes it appropriate to reduce the periodic reporting requirement that ATOMs file reports on volume and open interest four times a year with the NFA, to one annual report, filed by the ATOM with the Commission within 90 days of the end of its fiscal year, as proposed. Also as proposed, the Commission is retaining authority to obtain information as needed for regulatory purposes through inspections of the books and records of a particular firm and to conduct a market-wide survey, by special call, in order to evaluate the success of the rules. The information that would be required in a special call is specified in the rules.

The Commission is also revising, as proposed, the requirement that, except for funds used to purchase exchange-traded contracts as cover, ATOMs keep in segregation 100% of customer funds paid up front. In its rules governing the offer or sale of dealer options, another type of over-the-counter option, the Commission required the option grantor to hold not less than 90% of funds paid by a customer in segregation (17 CFR

32.6(a)). The Commission is applying that 90% requirement to agricultural trade options, as well. This will provide ATOMs with greater flexibility in structuring their businesses.

#### *D. Required Contract Terms and Limitations on Certain Strategies*

Commission final interim Rule 32.13(a)(6)(i)–(vii) required that agricultural trade option contracts specify a number of contract terms.<sup>20</sup> The Commission proposed to delete these design requirements on the grounds that the terms would be expected to be found in any fully-specified physical delivery option contract. Instead, the Commission proposed to include a statement in the Disclosure Document that option customers should be sure that the contract includes, and that the customer understands the operation of, all of the above contract provisions. The Commission believes that the proposal provides adequate customer protection while permitting ATOMs greater flexibility in specifying option contracts and is therefore adopting the change as final.

The Commission did not propose to change the existing requirement that a producer may write a call only to the extent that it is paired with a purchased or long put option in a window or fence strategy.<sup>21</sup> The Commission explained that, although some observers have suggested that producers, if they desire, should be able to grant or write call options if the position is covered by expected production, many producer representatives opposed changing the current requirement. As the Commission noted, this strategy:

[I]s not riskless. For example, if the producer suffers a production shortfall or loss, the producer's liability could be significant. For this reason, many of the producer representatives opposed changing the interim rules in this respect.

Id.

Two commenters in addition to the nine producer organizations supported continuation of the prohibition against producers writing covered calls. Others disagreed, suggesting that the

<sup>20</sup> These terms included the procedure for exercise, the expiration date and latest time on that date for exercise; the strike price; the total quantity of the commodity underlying the option; the quality or grade of commodity to be delivered if the option is exercised and any adjustments to price for deviations from stated quality or grade, or the range of, and a statement of the method for calculating such adjustments; the delivery location; the elements comprising the purchase price to be charged, including the premium, mark-ups on the premium, costs, fees and other charges; and additional costs, if any, which may be incurred if the commodity option is exercised.

<sup>21</sup> See 64 FR 47456.

prohibition against producers writing covered call options should be lifted to allow the greatest flexibility possible in formulating risk management strategies. As explained by one trade association, “[w]e believe the prohibition is an unnecessary restriction and could reduce the profit potential for an agricultural business and limit the potential for managing commodity price risk.”<sup>22</sup>

After careful consideration of the comments on this proposal, the Commission remains convinced that the current prohibition permitting call writing by producers only to the extent that the written call is paired with a purchased or long put option in a window or fence strategy should not be revised at this time. As the Commission stated in the proposed rulemaking, however, “[i]n taking this position, the Commission is not ruling out its reconsideration after producers have had an opportunity to gain experience generally with the offer and sale of trade options.” 64 FR 47456.

#### *E. Exemption Level for Sophisticated Entities*

The interim rules exempted transactions in which each party to the option contract had a net worth of not less than \$10 million from compliance with all of the specific conditions for trading agricultural trade options. The Commission determined that the exemption should apply only to those entities with a very high net worth and that a greater level of regulatory protection was appropriate for transactions involving less well-financed entities. In implementing the exemption for sophisticated entities, the Commission observed that there was no consensus among commenters regarding what the exemption level should be, or whether there should be an exemption at all.

Several commenters remarked on the current exemption level. Overall, there continues to be a lack of consensus regarding lowering the exemption level. Although some commenters advocated lowering the dollar amount of the exemption level, others, including the producer organizations opposed any exemption from the amended requirements or advocated maintaining the exemption at the current level. In light of the wide diversity of opinion, the untested nature of the rules, and the very broad changes already being made, the Commission continues to believe that the current exemption level should not be reduced at this time.

<sup>22</sup> See the letter of September 30, 1999 from the National Grain Trade Council to the CFTC.

### III. Other Matters

#### *A. Paperwork Reduction Act (PRA)*

Rules 3.13(e), 32.6, 32.13(a), 32.13(d), 32.13(e), 32.13(f)(1), 32.13(F)(2)–(5) and 32.13(c) contain information collection requirements. As required by the PRA of 1995 (Pub. L. 104–13 (May 13, 1996)), the Commission submitted a copy of the proposed rules and the associated paperwork burden to the Office of Management and Budget (OMB) for its review (44 U.S.C. 3504(h)) and requested comments on the paperwork burden from the public. The Commission did not receive comments addressing this specific associated paperwork burden. The Commission did receive and address, however, comments concerning the information that would be collected under the proposed rules.

OMB previously approved the collection of information related to these rules as information collection 3038–0048, Off-Exchange Agricultural Options. The final rules adopted by the Commission, which have been submitted to OMB for approval, have the following paperwork burden:

*Number of respondents:* 3,605.

*Estimated average hours per response:* 5.59.

*Frequency of response:* On occasion and annually.

*Number of responses per year:* 4,115.

*Annual reporting burden:* 23,003.

This represents a reduction of 9,045 burden hours as a result of the rule changes adopted. Persons wishing to comment on the paperwork burden contained in the final rules may contact the Desk Officer, CFTC, Office of Management and Budget, Room 10202, NEOB, Washington, DC 20503, (202) 395–7340. Copies of the information collection submission to OMB are available from the CFTC Clearance Officer, 1155 21st Street, NW, Washington, DC 20581, (202) 418–5160.

#### *B. Regulatory Flexibility Act (RFA)*

The RFA, 5 U.S.C. 601 *et seq.*, requires that agencies consider the impact of their rules on small businesses. The Commission has not previously determined whether all or some agricultural trade option merchants should be considered “small entities” for purposes of the RFA and, if so, to analyze the economic impact on such entities. However, the Commission is requiring one of the conditions for registration as an agricultural trade option merchant to be maintenance of a minimum level of net worth. The Commission previously found that other entities which were required to maintain minimum levels of net capital

were not small entities for purposes of the RFA. See, 47 FR 18618, 18619 (April 30, 1982). The Commission has also found, however, that one category of Commission registrant—introducing brokers (IBs)—which is required to maintain a minimum level of net capital, may include small entities for purposes of the RFA. Nevertheless, in addition to the \$50,000 minimum net worth required for registration as an agricultural trade option merchant, such registrants must be in business in the underlying cash commodity. This will require that they have additional resources invested in order to qualify as an agricultural trade option merchant, in contrast to an IB whose additional investment beyond the minimum net capital may be relatively small. For this reason, the Commission believes that agricultural trade option merchants are more appropriately treated as not being small entities under the RFA. The Chairman, on behalf of the Commission, hereby certifies, pursuant to 5 U.S.C. 605(b), that the action taken herein will not have a significant economic impact on a substantial number of small entities.

#### List of Subjects

##### 17 CFR Part 3

Administrative practice and procedure, Brokers, Commodity futures.

##### 17 CFR Part 32

Commodity futures, Commodity options, Prohibited transactions, Trade options.

In consideration of the foregoing, and pursuant to the authority contained in the Act, and in particular sections 2(a)(1)(A), 4c, and 8a, 7 U.S.C. 2, 6c, and 12A, as amended, the Commission hereby amends parts 3 and 32 of chapter I of title 17 of the Code of Federal Regulations as follows:

#### PART 3—REGISTRATION

1. The authority citation for part 3 continues to read as follows:

**Authority:** 7 U.S.C. 1a, 2, 4, 4a, 6, 6b, 6c, 6e, 6f, 6g, 6h, 6i, 6k, 6m, 6n, 6o, 6p, 8, 9, 9a, 12, 12a, 13b, 13c, 16a, 18, 19, 21, 23; 5 U.S.C. 552, 552b.

2. Section 3.13 is revised to read as follows:

##### § 3.13 Registration of agricultural trade option merchants and their associated persons.

(a) *Definitions.* (1) *Agricultural trade option merchant.* “Agricultural trade option merchant” means any person that is in the business of soliciting, offering to enter into, entering into, confirming the execution of, or

maintaining a position in, transactions or agreements in interstate commerce which are not conducted or executed on or subject to the rules of a contract market, and which are or are held out to be of the character of, or are commonly known to the trade as, an “option,” “privilege,” “indemnity,” “bid,” “offer,” “put,” “call,” “advance guarantee,” or “decline guarantee,” involving wheat, cotton, rice, corn, oats, barley, rye, flaxseed, grain sorghums, mill feeds, butter, eggs, solanum tuberosum (Irish potatoes), wool, wool tops, fats and oils (including lard, tallow, cottonseed oil, peanut oil, soybean oil and all other fats and oils), cottonseed meal, cottonseed, peanuts, soybeans, soybean meal, livestock, livestock products, and frozen concentrated orange juice. Provided, however, that any person entering into such transactions solely for the purpose of managing the risk arising from the conduct of his or her own commercial enterprise is not considered to be in the business described in this paragraph.

(2) Associated person of an agricultural trade option merchant. “Associated person of an agricultural trade option merchant” means a partner, employee, or agent (or any person occupying a similar status or performing similar functions) that:

(i) Solicits or accepts customers’ orders (other than in a clerical capacity) or

(ii) Supervises directly any person or persons so engaged.

(b) *Registration required.* It shall be unlawful for any person in the business of soliciting, offering or selling the instruments listed in § 32.2 of this chapter to solicit, to offer to enter into, or to enter into, to confirm the execution of, or to maintain transactions in such instruments or to supervise directly persons so engaged except if registered as an agricultural trade option merchant or as an associated person of such a registered agricultural trade option merchant under this section.

(c) *Duration of registration.* (1) A person registered in accordance with the provisions of this section shall continue to be registered until the revocation or withdrawal of registration.

(2) Agricultural trade option merchants must notify the National Futures Association within forty five days when an associated person has ceased to be so associated.

(3) An associated person who ceases to be associated with a registered agricultural trade option merchant is prohibited from engaging in activities requiring registration under § 32.13 of this chapter or representing himself or herself to be a registrant until:

(i) A registered agricultural trade option merchant notifies the National Futures Association of the person’s association; and

(ii) The associated person certifies to the National Futures Association that he or she is not disqualified from registration for the reasons listed in section 8a (2) and (3) of the Act; provided, however, no such certification is required when the associated person becomes associated with the new agricultural trade option merchant within ninety days from when the associated person ceased the previous association.

(d) *Conditions for registration.* (1) Applicants for registration as an agricultural trade option merchant must meet the following conditions:

(i) The agricultural trade option merchant must have and maintain at all times net worth of at least \$50,000 computed in accordance with generally accepted accounting principles;

(ii) The agricultural trade option merchant must identify each of the natural persons who controls or directs the offer or sale of trade options or associated trading activity by the agricultural trade option merchant and any associated person of the agricultural trade option merchant and each such natural person must certify that he or she is not disqualified from registration for the reasons listed in sections 8a(2) and (3) of the Act; and

(iii) The agricultural trade option merchant must provide access to any representative of the Commission or the United States Department of Justice for the purpose of inspecting books and records.

(2) Applicants for registration as an associated person of an must meet the following conditions. Such persons must:

(i) Identify the agricultural trade option merchant with whom the person is associated or to be associated within thirty days of the person’s registration; and

(ii) Certify that he or she is not disqualified from registration for the reasons listed in sections 8a(2) and (3) of the Act.

(e) *Applications for registration.* (1) The agricultural trade option merchant, including its principals, and associated persons of an agricultural trade option merchant must apply for registration on the appropriate forms specified by the National Futures Association and approved by the Commission, in accordance with the instructions thereto, including the separate certifications from each natural person that he or she is not disqualified for any of the reasons listed in sections 8a(2)

and (3) of the Act and such other identifying background information as may be specified.

(2) The agricultural trade option merchant's application must also include its most recent annual financial statements certified by an independent certified public accountant in accordance with generally accepted auditing standards prepared within the prior 12 months.

(3) These applications must be supplemented to include any changes in the information required to be provided thereon on a form specified by the National Futures Association and approved by the Commission.

(f) *Withdrawal of application for registration; denial, suspension and revocation of registration.* The provisions of §§ 3.51, 3.55, 3.56 and 3.60 shall apply to applicants for registration and registrants as agricultural trade options merchants and their associated persons under this part 3 as though they were an applicant or registrant in any capacity under the Act.

(g) *Withdrawal from registration.* An agricultural trade option merchant that has ceased or has not commenced engaging in activities requiring registration may withdraw from registration 30 days after notifying the National Futures Association on the specified form of its intent to do so, unless otherwise notified by the Commission. Such a withdrawal notification must include information identifying the location of, and the custodian authorized to release, the agricultural trade option merchant's records, a statement of the disposition of customer positions, cash balances, securities or other property and a statement that no obligations to customers arising from agricultural trade options remain outstanding.

(h) *Dual registration of associated persons.* An associated person of an agricultural trade option merchant may be associated with other registrants subject to the provision of § 3.12(f).

3. Section 3.14 is removed and reserved.

## PART 32—REGULATION OF COMMODITY OPTION TRANSACTIONS

4. The authority citation for part 32 continues to read as follows:

**Authority:** 7 U.S.C. 2, 6c and 12a.

5. Section 32.2 is republished for the convenience of the reader:

### § 32.2 Prohibited transactions.

Notwithstanding the provisions of § 32.11, no person may offer to enter into, confirm the execution of, or

maintain a position in, any transaction in interstate commerce involving wheat, cotton, rice, corn, oats, barley, rye, flaxseed, grain sorghums, mill feeds, butter, eggs, solanum tuberosum (Irish potatoes), wool, wool tops, fats and oils (including lard, tallow, cottonseed oil, peanut oil, soybean oil and all other fats and oils), cottonseed meal, cottonseed, peanuts, soybeans, soybean meal, livestock, livestock products, and frozen concentrated orange juice if the transaction is or is held out to be of the character of, or is commonly known to the trade as an "option," "privilege," "indemnity," "bid," "offer," "put," "call," "advance guarantee," or "decline guarantee," except as provided under § 32.13 of this part.

6. Section 32.13 is revised to read as follows:

### § 32.13 Exemption from prohibition of commodity option transactions for trade options on certain agricultural commodities.

(a) The provisions of § 32.11 shall not apply to the solicitation or acceptance of orders for, or the acceptance of money, securities or property in connection with, the purchase or sale of any commodity option on a physical commodity listed in § 32.2 by a person who is a producer, processor, or commercial user of, or a merchant handling or selling inputs used in the production of, the commodity which is the subject of the commodity option transaction, or the products or byproducts thereof, or a bank routinely engaged in the financing of such businesses, if all of the following conditions are met at the time of the solicitation or acceptance:

(1) That person is registered with the Commission as an agricultural trade option merchant and that person's associated persons and their supervisors are registered as associated persons of an agricultural trade option merchant under § 3.13 of this chapter.

(2) The option offered by the agricultural trade option merchant is offered to a producer, processor, or commercial user of, or a merchant handling, the commodity which is the subject of the commodity option transaction, or the products or byproducts thereof, and such producer, processor, commercial user, or merchant is offered or enters into the commodity option transaction solely for purposes related to its business as such.

(3) [Reserved]

(4) To the extent that the customer makes payment of the purchase price to the agricultural trade option merchant prior to option expiration or exercise, that amount:

(i) May only be used by the agricultural trade option merchant to purchase a covering position on a contract market designated under section 6 of the Act or part 33 of this chapter; and

(ii) Any amount not so used shall be treated as belonging to the customer until option expiration or exercise as provided under and in accordance with § 32.6.

(5) Producers may not:

(i) Grant or sell a put option; or

(ii) Grant or sell a call option, except to the extent that such a call option is purchased or combined with a purchased or long put option position, and only to the extent that the customer's call option position does not exceed the customer's put option position in the amount to be delivered. Provided, however, that the options must be entered into simultaneously and expire simultaneously or at any time that one or the other option is exercised.

(6) All option contracts, including all terms and conditions, offered or sold pursuant to this section shall be in writing, a signed copy of which shall be provided to the customer, or if the contract is verbal, it shall be confirmed in a writing which includes all terms and conditions, signed by the agricultural trade option merchant, and provided to the customer within 48 hours.

(7) Prior to the entry by a customer into the first option transaction with an agricultural trade option merchant, the agricultural trade option merchant shall furnish, through written or electronic media, a summary disclosure statement to the option customer. The summary disclosure statement shall include:

(i) The following statements in boldface type on the first page(s) of the summary disclosure statement:

This brief statement does not disclose all of the risks and other significant aspects of trading in commodity trade options. You are encouraged to seek out as much information as possible from sources other than the person selling you this option about the use and risks of option contracts before entering into this contract. The issuer of your option should be willing and able to answer clearly any of your questions.

### Appropriateness of Option Contracts

Option contracts may result in the total loss of any funds you pay to the issuer of your option. You should carefully consider whether trading in such instruments is appropriate for you in light of your experience, objectives, financial resources and other relevant circumstances. The issuer of your option contract should be willing and able to explain the financial outcome of your option contract under different market conditions. You should also be aware that

this option is not issued by, guaranteed by, or traded on or subject to the rules of a futures exchange. You may be able to obtain a similar contract or execute a similar risk management strategy using an instrument traded on a futures exchange which offers greater regulatory and financial protections.

#### Costs and Fees Associated With an Option Contract

Before entering into an option contract, you should understand all of the costs associated with it. These include the option premium, commissions, fees, costs associated with delivery if the option requires settlement by delivery upon its exercise and any other charges which may be incurred. All of these costs and fees must be specified in the terms of your option contract.

#### Know and Understand the Terms of the Option Contract

Before entering into an option contract, you should know and understand all of the option contract's terms. All of the option contract's terms should be included in the written contract, or for a verbal agreement, in a written confirmation. You should receive a signed copy of either the written contract or of the written confirmation. Your option contract should include contract terms setting:

- (A) The total quantity of commodity underlying the option contract;
- (B) The strike price(s) of the option contract;
- (C) The procedure for exercise of the option contract, including when you can exercise and the latest time and date for exercise;
- (D) Whether the option can be offset or canceled prior to expiration;
- (E) Whether settlement of the option is for cash or by delivery of the commodity;
- (F) If settlement is by delivery, the delivery location or locations, the quality or grade of commodity to be delivered and how adjustments to price for deviations from stated quality or grade are determined;
- (G) If settlement is by cash, the method for determining the cash-settlement price; and
- (H) The cost and method of payment.

#### Business Use of Trade Options

In order to comply with the law, you must be buying this option for business-related purposes. The terms and structure of the contracts must therefore relate to your activity or commitments in the underlying cash market. Any amendments allowed to the option contract or its cancellation or offset prior to its expiration date must reflect changes in your activity, in your commitments in the underlying cash market or in the carrying of inventory. Producers are not permitted to enter into short call options unless the producer also enters into a long put option contract for the same amount or more of the commodity, at the same time and with the same expiration date. Producers are not permitted to sell put options, whether alone or in combination with a call option.

#### Dispute Resolution

If a dispute should arise under the terms of this trade option contract, you have the right to choose to use the reparations

program run by the Commodity Futures Trading Commission or any other dispute resolution forum provided to you under the terms of your customer agreement or by law. For more information on the Commission's Reparations Program contact: Office of Proceedings, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW, Washington, DC 20581, (202) 418-5250.

#### Acknowledgment of Receipt

The Commodity Futures Trading Commission requires that all customers receive and acknowledge receipt of this disclosure statement. The Commodity Futures Trading Commission does not intend this statement as a recommendation or endorsement of agricultural trade options. These commodity options have not been approved or disapproved by the Commodity Futures Trading Commission, nor has the Commission passed upon the accuracy or adequacy of this disclosure statement. Any representation to the contrary is a violation of the Commodity Exchange Act and Federal regulations.

(ii) The following acknowledgment section:

I hereby acknowledge that I have received and understood this summary risk disclosure statement.

(Date)

Signature of Customer

(8) An agricultural trade option merchant may not require a customer to waive the right to seek reparations under section 14 of the Act and part 12 of this chapter by an agreement or understanding to submit a claim or grievance to a specified settlement procedure prior to the time a claim or grievance arises. An agricultural trade option merchant, when notifying a customer of its intent to submit a claim or grievance to arbitration under a pre-existing agreement, must advise the customer in writing that the customer within forty-five days may elect to seek reparations under Section 14 of the Act and part 12 of this chapter.

(b) *Report of account information.* Agricultural trade option merchants must provide to customers with open positions the following information:

(1) Within two business days of the offset, cancellation or settlement of the option for cash, or of the amendment of the expiration of the option, a statement of profit or loss on the transaction and on the account;

(2) In response to a customer's request, current commodity price quotes, all other information relevant to the customer's position or account, and the amount of any funds owed by, or to, the customer within one business day if responding orally and within two business days if responding in writing;

(3) Written, verbal or electronic notice of the expiration date of each option which will expire within the subsequent calendar month.

(c) *Recordkeeping.* Agricultural trade option merchants shall keep full, complete and systematic books and records together with all pertinent data and memoranda of or relating to agricultural trade option transactions, covering transactions, and all written or electronic customer solicitation materials. Agricultural trade option merchants shall maintain such books and records as specified in § 1.31 of this chapter, and report to the Commission as provided for in this paragraph (c) and paragraph (d) of this section and as the Commission may otherwise require by rule, regulation, or order. Such books and records shall be open at all times to inspection by any representative of the Commission and the United States Department of Justice.

(d) *Reports.* Agricultural trade option merchants must file annual reports with the Commission at its Washington, DC, headquarters within ninety days after the close of the agricultural trade option merchant's fiscal year, in the form and manner specified by the Commission, which shall contain the following information:

- (1) By commodity and put, call or combined option
  - (i) Total number of new contracts entered into during the reporting period;
  - (ii) Total quantity of commodity underlying new contracts entered into during the reporting period;
  - (iii) Total number of contracts outstanding at the end of the reporting period;
  - (iv) Total quantity of underlying commodity outstanding under option contracts at the end of the reporting period;
  - (v) Total number of options exercised during the reporting period; and
  - (vi) Total quantity of commodity underlying the options exercised during the reporting period.

(2) Total number of customers by commodity with open option contracts at the end of the reporting period.

(e) *Special calls.* Upon special call by the Commission for information relating to agricultural trade options offered or sold on the dates specified in the call, each agricultural trade option merchant shall furnish to the Commission within the time specified the following information as specified in the call:

(1) All positions and transactions in agricultural trade options, including information on the identity of agricultural trade option customers and on the value of premiums, fees, commissions, or charges other than



option premiums, collected on such transactions.

(2) All related positions and transactions for future delivery or options on contracts for future delivery or on physicals on all contract markets.

(3) All related positions and transactions in cash commodities, their products, and by-products.

(f) *Internal controls.* (1) Each agricultural trade option merchant registered with the Commission shall prepare, maintain and preserve information relating to its written policies, procedures, or systems concerning the agricultural trade option merchant's internal controls with respect to market risk, credit risk, and other risks created by the agricultural trade option merchant's activities, including systems and policies for supervising, monitoring, reporting and reviewing trading activities in agricultural trade options; policies for hedging or managing risk created by trading activities in agricultural trade options, including a description of the types of reviews conducted to monitor positions; and policies relating to restrictions or limitations on trading activities.

(2) The financial statements of the agricultural trade option merchant must on an annual basis be audited by a certified public accountant in accordance with generally accepted auditing standards.

(3) The agricultural trade option merchant must file with the Commission a copy of its certified financial statements within 90 days after the close of the agricultural trade option merchant's fiscal year.

(4) The agricultural trade option merchant must perform a reconciliation of its books at least monthly.

(5) The agricultural trade option merchant:

(i) Must report immediately if its net worth falls below the level prescribed in § 3.13(d)(1)(i) of this chapter, and must report within three days discovery of a material inadequacy in its financial statements by an independent public accountant or any state or federal agency performing an audit of its financial statements, such report to be made to the Commission by facsimile, telegraphic or other similar electronic notice; and

(ii) Within five business days after giving such notice, the agricultural trade option merchant must file a written report with the Commission stating what steps have been taken or are being taken to correct the material inadequacy.

(6) If the agricultural trade option merchant's net worth falls below the

level prescribed in § 3.13(d)(1)(i) of this chapter, it must immediately cease offering or entering into new option transactions and must notify customers having premiums which the agricultural trade option merchant is holding under paragraph (a)(4) of this section that such customers can obtain an immediate refund of that premium amount, thereby closing the option position.

(g) *Exemption.*

(1) The provisions of §§ 3.13, 32.2, 32.11 of this chapter and this section shall not apply to a commodity option offered by a person which has a reasonable basis to believe that:

(i) The option is offered to a producer, processor, or commercial user of, or a merchant handling, the commodity which is the subject of the commodity option transaction, or the products or byproducts thereof;

(ii) Such producer, processor, commercial user or merchant is offered or enters into the commodity option transaction solely for purposes related to its business as such; and

(iii) Each party to the option contract has a net worth of not less than \$10 million or the party's obligations on the option are guaranteed by a person which has a net worth of \$10 million and has a majority ownership interest in, is owned by, or is under common ownership with, the party to the option.

(2) Provided, however, that § 32.9 continues to apply to such option transactions.

Issued this 29th day of November, 1999, in Washington, DC, by the Commodity Futures Trading Commission.

**Jean A. Webb,**

*Secretary of the Commission.*

[FR Doc. 99-31453 Filed 12-3-99; 8:45 am]

**BILLING CODE 6351-01-P**

## SECURITIES AND EXCHANGE COMMISSION

### 17 CFR Part 270

[Release Nos. IC-24177, IA-1846; File No. S7-22-98]

RIN 3235-AH02

### Temporary Exemption for Certain Investment Advisers

**AGENCY:** Securities and Exchange Commission.

**ACTION:** Final rule.

**SUMMARY:** The Commission is adopting amendments to the rule under the Investment Company Act of 1940 that permits an investment adviser to advise an investment company under a temporary contract that the investment

company's shareholders have not approved. The amendments expand the circumstances in which the exemption provided by the rule is available, to include a merger or similar business combination involving an investment company's adviser. The amendments also lengthen the maximum duration of the temporary contract. The amendments will permit more investment advisers to rely on the rule rather than seek individual exemptions from the Commission, and will continue to protect the interests of investors pending their vote on a new advisory contract.

**EFFECTIVE DATE:** The rule amendments will be effective December 13, 1999.

**FOR FURTHER INFORMATION CONTACT:**

Penelope W. Saltzman, Senior Counsel, (202) 942-0690, or C. Hunter Jones, Assistant Director, Office of Regulatory Policy, Division of Investment Management, Securities and Exchange Commission, 450 Fifth Street, NW, Washington, DC 20549-0506.

**SUPPLEMENTARY INFORMATION:** The Securities and Exchange Commission (the "Commission") today is adopting amendments to rule 15a-4 (17 CFR 270.15a-4) under the Investment Company Act of 1940 (15 U.S.C. 80a) (the "Investment Company Act" or the "Act").<sup>1</sup>

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### I. Executive Summary

The Commission is adopting amendments to rule 15a-4 under the Investment Company Act, the rule that permits an investment adviser to an investment company ("fund") to serve for a short period of time under a contract that shareholders have not approved ("interim contract"). The amendments expand and clarify coverage of the rule by:

- Clarifying the timing of the board of directors' approval of the interim contract;

<sup>1</sup> Unless otherwise noted, all references to "amended rule 15a-4," "rule 15a-4, as amended," or any paragraph of the rule will be to 17 CFR 270.15a-4, as amended by this release.