numerous reports of cracked valves that have not yet failed.

Two major failure modes of this valve have been identified. One involves improper assembly of the valve by the manufacturer, whereby insufficient torque is applied to the nut which holds the valve poppet assembly together. The other failure mode involves fatigue cracks of the poppet itself. Since the first failure mode may exist in brand-new valves, an initial inspection is required to check for loose bolts and nuts. The fatigue cracks develop and progress with time, and this failure mode is thus addressed by a repetitive inspection requirement. The same inspection procedure is called out in the AD for both the initial and repetitive inspections, since it is possible that fatigue cracks could be discovered on the initial inspection, and an improperly torqued nut could be found to be loose on a later inspection. The inspection procedure allows for both possibilities.

The direction that valve fragments would travel through the pneumatic duct in the event of valve failure changes several times during a given flight, and is determined by the automatic switchover of bleed air sources by the pneumatic system. At high engine power settings, such as during takeoff and climb, the airplane is being supplied bleed air from the low-pressure bleed source, and any fragments from a failed check valve would be carried away from the engine, and into the pneumatic system. At low engine power settings, such as at some cruise conditions and descent, there is insufficient bleed air available from the low-pressure source, and a high-pressure bleed valve automatically opens. The check valve discussed herein is designed to prevent this high pressure air from re-entering the engine through the low-pressure port. If the check valve should fail in this situation, valve fragments would be swept into the engine, or, if the valve had failed earlier in the flight, high-pressure bleed air would not be prevented from re-entering the engine. This could result in a compressor stall or other engine abnormalities.

On January 17, 1986, The Boeing Company issued Service Bulletin 767-36-0017, which describes inspection and repair procedures applicable to the subject valve.

Terminating action for this AD, which will require a design change to the valve, has not been identified at this time.

Since this condition is likely to exist or develop on other airplanes of this model, the FAA has determined that an AD is necessary which requires inspection, and, as necessary, repair or replacement of all pneumatic system 8th stage check valves in accordance with the service bulletin previously mentioned.

Further, since a situation exists that requires immediate adoption of this regulation, it is found that notice and public procedure hereon are impracticable, and good cause exists for making this amendment effective in less than 30 days.

Although this action is in the form of a final rule, which involves an emergency and, thus, was not preceded by notice and public procedure, interested persons are invited to submit such written data, views, or arguments as they may desire regarding this AD. Communications should identify the docket number and be submitted in duplicate to the Federal Aviation Administration, Northwest Mountain Region, Office of the Regional Counsel, Attention: Airworthiness Directives Rules Docket No. 86-NM-14-AD, 17900 Pacific Highway South, C-68966, Seattle, Washington 98168. All communications received before the closing date will be considered by the Administrator, and the AD may be changed in light of the comments received.

The FAA has determined that this regulation is an emergency regulation that is not major under Executive Order 12291. It is impracticable for the agency to follow the procedures of Order 12291 with respect to this rule since the rule must be issued immediately to correct an unsafe condition in aircraft. It has been further determined that this document involves an emergency regulation under DOT Regulatory Policies and Procedures (44 FR 11034; February 26, 1979). If this action is subsequently determined to involve a significant/major regulation, a final regulatory evaluation or analysis, as appropriate, will be prepared and placed in the regulatory docket (otherwise, an evaluation or analysis is not required).

List of Subjects in 14 CFR Part 39

Aviation safety, Aircraft.

Adoption of the Amendment

PART 39—[AMENDED]

Accordingly, pursuant to the authority delegated to me by the Administrator, the Federal Aviation Administration amends § 39.13 of Part 39 of the Federal Aviation Regulations as follows:

1. The authority citation for Part 39 continues to read as follows:

Authority: 49 U.S.C. 1354(a), 1421 and 1423; 49 U.S.C. 106(g) (Revised Pub. L. 97-449, January 12, 1983); and 14 CFR 11.89.

2. By adding the following new airworthiness directive:

Boeing: Applies to all Model 767 airplanes, certificated in any category. Compliance is required as stated below. To preclude engine or pneumatic system damage caused by the failure of the pneumatic system 8th stage check valve, Hamilton Standard Part Number 773856-3, accomplish the following, unless already accomplished:

A. Within 500 hours time in service after the effective date of this AD, inspect the pneumatic system 8th stage check valve, Hamilton Standard Part Number 773856-3, in accordance with Boeing Service Bulletin 767-36-0017, dated January 17, 1986, or later FAA-approved revisions. If the valve contains any visible cracks, or exceeds the allowable wear limits specified in the reference service bulletin, repair the valve in accordance with the referenced service bulletin, or replace the valve with a servicable valve before further flight. Valves not installed on an airplane must be inspected prior to their installation.

B. Repeat the inspection procedures in paragraph A., above, at intervals not to exceed 2,000 hours time in service.

C. Alternate means of compliance which provide an acceptable level of safety may be used when approved by the Manager, Seattle Aircraft Certification Office, FAA, Northwest Mountain Region.

D. Special flight permits may be issued in accordance with FAR 21.197 and 21.199 to operate airplanes to a base for the accomplishment of inspections and/or modifications required by this AD.

All persons affected by this AD who have not already received copies of the Service Bulletin cited herein may obtain copies upon request from the Boeing Commercial Airplane Company, P.O. Box 3707, Seattle, Washington 98124. These documents may be examined at the FAA, Northwest Mountain Region, 17900 Pacific Highway South, Seattle, Washington, or the Seattle Aircraft Certification Office, 9010 East Marginal Way South, Seattle, Washington.

This amendment becomes effective April 1, 1986.

Issued in Seattle, Washington, on March 7, 1986.

Charles R. Foster,

Director, Northwest Mountain Region.

[FR Doc. 86-5570 Filed 3-13-86; 8:45 am]

BILLING CODE 4910-13-M

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14 CFR Part 97

[Docket No. 24935; Amdt. No. 1316]

Standard Instrument Approach Procedures; Miscellaneous Amendments

AGENCY: Federal Aviation Administration (FAA), DOT.

ACTION: Final rule.

SUMMARY: This amendment establishes, amends, suspends, or revokes Standard Instrument Approach Procedures (SIAPs) for operations at certain airports. These regulatory actions are needed because of the adoption of new or revised criteria, or because of changes occurring in the National Airspace System, such as the commissioning of new navigational facilities, addition of new obstacles, or changes in air traffic requirements. These changes are designed to provide safe and efficient use of the navigable airspace and to promote safe flight operations under instrument flight rules at the affected airports.

DATES: Effective: An effective date for each SIAP is specified in the amendatory provisions.

Incorporation by reference—approved by the Director of the Federal Register on December 31, 1980, and reapproved as of January 1, 1982.

ADDRESSES: Availability of matters incorporated by reference in the amendment is as follows:

For Examination:

1. FAA Rules Docket, FAA Headquarters Building, 800 Independence Avenue, SW., Washington, DC 20591;

2. The FAA Regional Office of the region in which the affected airport is located; or

3. The Flight Inspection Field Office which originated the SIAP.

For Purchase:

Individual SIAP copies may be obtained from:

1. FAA Public Inquiry Center (APA-430), FAA Headquarters Building, 800 Independence Avenue, SW., Washington, DC 20591; or

2. The FAA Regional Office of the region in which the affected airport is located.

By Subscription:

Copies of all SIAPs, mailed once every 2 weeks, are for sale by the Superintendent of Documents, U.S. Government Printing Office, Washington, DC 20402.

FOR FURTHER INFORMATION CONTACT: Donald K. Funai, Flight Procedures Standards Branch (AFO-230), Air Transportation Division, Office of Flight Operations, Federal Aviation Administration, 800 Independence Avenue, SW., Washington, DC 20591; telephone (202) 426-8277.

SUPPLEMENTARY INFORMATION:

This amendment to Part 97 of the Federal Aviation Regulations (14 CFR Part 97) prescribes new, amended, suspended, or revoked Standard Instrument Approach Procedures (SIAPs). The complete regulatory description of each SIAP is contained in official FAA form documents which are incorporated by reference in this amendment under 5 U.S.C. 552(a), 1 CFR Part 51, and § 97.20 of the Federal Aviation Regulations (FARs). The applicable FAA Forms are identified as FAA Forms 8260-3, 8260-4, and 8260-5. Materials incorporated by reference are available for examination or purchase as stated above.

The large number of SIAPs, their complex nature, and the need for a special format make their verbatim publication in the **Federal Register** expensive and impractical. Further, airmen do not use the regulatory text of the SIAPs, but refer to their graphic depiction on charts printed by publishers of aeronautical materials. Thus, the advantages of incorporation by reference are realized and publication of the complete description of each SIAP contained in FAA form document is unnecessary. The provisions of this amendment state the affected CFR (and FAR) sections, with the types and effective dates of the SIAPs. This amendment also identifies the airport, its location, the procedure identification and the amendment number. This amendment to Part 97 is effective on the date of publication and contains separate SIAPs which have compliance dates stated as effective dates based on related changes in the National Airspace System or the application of new or revised criteria. Some SIAP amendments may have been previously issued by the FAA in a National Flight Data Center (FDC) Notice to Airmen (NOTAM) as an emergency action of immediate flight safety relating directly to published aeronautical charts. The circumstances which created the need for some SIAP amendments may require making them effective in less than 30 days. For the remaining SIAPs, an effective date at least 30 days after publication is provided.

Further, the SIAPs contained in this amendment are based on the criteria contained in the U.S. Standard for Terminal Instrument Approach Procedures (TERPs). In developing these SIAPs, the TERPS criteria were applied to the conditions existing or anticipated at the affected airports. Because of the close and immediate relationship between these SIAPs and safety in air commerce, I find that notice and public procedure before adopting these SIAPs is unnecessary, impracticable, and contrary to the public interest and, where applicable, that good cause exists for making some SIAPs effective in less than 30 days.

The FAA has determined that this regulation only involves an established body of technical regulations for which frequent and routine amendments are necessary to keep them operationally current. It, therefore, (1) is not a "major rule" under Executive Order 12291; (2) is not a "significant rule" under DOT Regulatory Policies and Procedures (44 FR 11034; February 26, 1979); and (3) does not warrant preparation of a regulatory evaluation as the anticipated impact is so minimal. For the same reason, the FAA certifies that this amendment will not have a significant economic impact on a substantial number of small entities under the criteria of the Regulatory Flexibility Act.

List of Subjects in 14 CFR Part 97

Aviation safety, Approaches, Standard instrument, Incorporation by reference.

Issued in Washington, DC on March 7, 1986.

John S. Kern,

Acting Director of Flight Standards.

Adoption of the Amendment

PART 97—[AMENDED]

Accordingly, pursuant to the authority delegated to me, Part 97 of the Federal Aviation Regulations (14 CFR Part 97) is amended by establishing, amending, suspending, or revoking Standard Instrument Approach Procedures, effective at 0901 G.M.T. on the dates specified, as follows:

1. The authority citation for Part 97 continues to read as follows:

Authority: 49 U.S.C. 1348, 1354(a), 1421, and 1510; 49 U.S.C. 106(g) (revised, Pub. L. 97-449, January 12, 1983; and 14 CFR 11.49(b)(2)).

By amending: § 97.23 VOR, VOR/DME, VOR or TACAN, and VOR/DME or TACAN; § 97.25 LOC, LOC/DME, LDA, LDA/DME, SDF, SDF/DME; § 97.27 NDB, NDB/DME; § 97.29 ILS, ILS/DME, ISMLS, MLS, MLS/DME, MLS/RNAV; § 97.31 RADAR SIAPs; § 97.33 RNAV SIAPs; and § 97.35 COPTER SIAPs, identified as follows:

. . . **Effective 8 May 1986**

Camden, AR—Harrell Field, VOR/DME RWY 18, Amdt. 3, Cancelled

Hot Springs—AR, Memorial Field, VOR-1 RWY 5, Amdt. 14

Hot Springs—AR, Memorial Field, VOR-2 RWY 5, Amdt. 2

Hot Springs—AR, Memorial Field, ILS RWY 5, Amdt. 11

Kahului, HI—Kahului, VOR/DME or TACAN RWY 20, Amdt. 5

Kahului, HI—Kahului, VOR/DME or TACAN-A, Amdt. 5

Kahului, HI—Kahului, LOC/DME (BC) RWY 20, Amdt. 9

Connersville, IN—Mettel Field, VOR/DME–A, Amdt. 5
Connersville, IN—Mettel Field, NDB RWY 18, Amdt. 9
Connersville, IN—Mettel Field, RNAV RWY 18, Amdt. 5
New Castle, IN—New Castle-Henry County Muni., NDB RWY 9, Amdt. 4
New Castle, IN—New Castle-Henry County Muni., NDB RWY 27, Amdt. 4
Richmond, IN—Richmond Muni, VOR RWY 6, Amdt. 9
Richmond, IN—Richmond Muni, VOR RWY 24, Amdt. 9
Winchester, IN—Randolph County, VOR–A, Amdt. 7
Winchester, IN—Randolph County, NDB RWY 25, Amdt. 3
Davenport, IA—Davenport Muni, NDB RWY 3, Amdt. 13, Cancelled
Hastings, MI—Hastings, VOR RWY 12, Amdt. 7
Houghton Lake, MI—Roscommon County, VOR RWY 27, Orig.
Sidney, MT—Sidney-Richland Muni, NDB RWY 1, Amdt. 1
Sidney, MT—Sidney-Richland Muni, NDB RWY 19, Amdt. 2
Farmington, NM—Four Corners Regional, VOR/DME RWY 7, Amdt. 2
Reno, NV—Reno Cannon Intl, VOR/DME RWY 34L, Orig.
Dayton, OH—Dayton General Arpt South, VOR RWY 20, Amdt. 7
Dayton, OH—Dayton General Arpt South, VOR A, Amdt. 11
Dayton, OH—Dayton General Arpt South, NDB RWY 9, Amdt. 5
Dayton, OH—James Cox Dayton Intl, NDB RWY 6R, Amdt. 5
Dayton, OH—James Cox Dayton Intl, RNAV RWY 6R, Amdt. 6
Harrison, OH—Harrison, VOR RWY 18, Amdt. 1
Lebanon, OH—Lebanon-Warren County, NDB–A, Amdt. 3
Brookings, SD—Brookings Muni, VOR RWY 12, Amdt. 7
Brookings, SD—Brookings Muni, VOR RWY 30, Amdt. 5
Houston, TX—Houston-Hull Field, LOC RWY 35, Amdt. 1, Cancelled
Houston, TX—Houston-Hull Field, ILS RWY 35, Orig
Killeen, TX—Killeen Muni, VOR–A, Amdt. 1
Appleton, WI—Outagamie County, VOR/DME RWY 3, Amdt. 3
Appleton, WI—Outagamie County, LOC BC RWY 21, Amdt. 4
Appleton, WI—Outagamie County, NDB RWY 3, Amdt. 10
Appleton, WI—Outagamie County, NDB RWY 11, Amdt. 3
Appleton, WI—Outagamie County, NDB RWY 29, Amdt. 3
Appleton, WI—Outagamie County, ILS RWY 3, Amdt. 12
Appleton, WI—Outagamie County, RNAV RWY 29, Amdt. 3
Delavan, WI—Lake Lawn, NDB RWY 18, Amdt. 2
Manitowoc, WI—Manitowoc County, VOR RWY 35, Amdt. 10
Oconto, WI—Oconto Muni, NDB RWY 11, Amdt. 4

. . . Effective 10 April 1986

Butler, AL—Butler-Choctaw County, NDB RWY 11, Amdt. 1
Key West, FL—Key West Intl, RADAR–1, Amdt. 2
Miami, FL—Miami Intl, RADAR–1, Amdt. 21, Cancelled
Monroe, GA—Monroe-Walton County, NDB RWY 3, Amdt. 1
Thomasville, GA—Thomasville Muni, VOR/RWY 22, Amdt. 10
Thomasville, GA—Thomasville Muni, VOR/DME RWY 22, Amdt. 4
Thomasville, GA—Thomasville Muni, LOC RWY 22, Amdt. 2
Thomasville, GA—Thomasville Muni, NDB RWY 22, Amdt. 2
Thomasville, GA—Thomasville Muni, RNAV RWY 32, Amdt. 3
Winder, GA—Winder, LOC RWY 31, Amdt. 7
Winder, GA—Winder, NDB RWY, Amdt. 7
Mount Sterling, KY—Mt Sterling-Montgomery County, VOR RWY 7, Amdt. 2, Cancelled
Mount Sterling, KY—Mt Sterling-Montgomery County, VOR/DME RWY 7, Amdt. 32, Cancelled
Mount Sterling, KY—Mt Sterling-Montgomery County, VOR A, Orig
Mount Sterling, KY—Mt Sterling-Montgomery County, VOR/DME–B, Orig
Baton Rouge, LA—Baton Rouge Metropolitan, Ryan Field, LOC BC RWY 4, Orig.
Houlton, ME—Houlton Intl, VOR RWY 5, Amdt. 8
Baltimore, MD—Baltimore-Washington Intl, RNAV RWY 22, Amdt. 6
Oakland, MD—Garrett County, VOR RWY 26, Amdt. 3
Fayetteville, NC—Fayetteville Muni (Grannis Fld), VOR RWY 4, Amdt. 15
Fayetteville, NC—Fayetteville Muni (Grannis Fld), VOR RWY 22, Amdt. 4
Fayetteville, NC—Fayetteville Muni (Grannis Fld), VOR RWY 28, Amdt. 6
Fayetteville, NC—Fayetteville Muni (Grannis Fld), LOC BC RWY 22, Amdt. 5
Fayetteville, NC—Fayetteville Muni (Grannis Fld), NDB RWY 4, Amdt. 14
Fayetteville, NC—Fayetteville Muni (Grannis Fld), ILS RWY 4, Amdt. 14
Fayetteville, NC—Fayetteville Muni (Grannis Fld), RADAR–1, Amdt. 4
Sanford, NC—Sanford-Lee County Brick Field, NDB RWY 3, Orig.
West Jefferson, NC—Ashe County, NDB RWY 27, Admt. 1
Mandan, ND—Mandan Muni, RADAR–1, Amdt. 1
Beaufort, SC—Beaufort County, RADAR–1, Amdt. 1
Laredo, TX—Laredo Intl, LOC BC RWY 35L, Orig., Cancelled

. . . Effective 20 February 1986

Russellville, AR—Russellville Muni, NDB–A, Amdt. 3

[FR Doc. 86–5572 Filed 3–13–86; 8:45 am]

BILLING CODE 4910-13-M

SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 240

[Release No. 34–22979; File No. S7–36–84]

Exemption of Certain Direct Participation Program Securities

AGENCY: Securities and Exchange Commission.

ACTION: Final rule.

SUMMARY: The Commission is adopting Rule 3a12–9 under the Securities Exchange Act of 1934 ("Exchange Act"). The Rule exempts the securities of certain direct participation programs from the "arranging" provisions of sections 7(c) and 11(d)(1) of the Exchange Act. The Rule will thus allow broker-dealers to participate in public offerings of the securities of direct participation programs with mandatory deferred payments, provided that certain conditions are met. The Commission does not believe that public offerings which meet the requirements of the Rule present the potential for abuse which sections 7(c) and 11(d)(1) were designed to prevent.

EFFECTIVE DATE: April 14, 1986.

FOR FURTHER INFORMATION CONTACT: Edward L. Pittman, Esq., (202) 272–2848; Office of Chief Counsel, Division of Market Regulation, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549.

SUPPLEMENTARY INFORMATION:

I. Introduction

The Commission today announced the adoption of Rule 3a12–9 (17 CFR 240.3a12–9) under the Exchange Act.[1] The Rule was published for comment in November, 1984.[2] Pursuant to section 3(a)(12) of the Exchange Act, the Rule provides that interests in certain direct participation programs[3] are exempted securities for purposes of the arranging for credit provisions of sections 7(c) and 11(d)(1) of the Exchange Act.[4] The Rule

[1] 15 U.S.C. 78a *et. seq.*

[2] Securities Exchange Act Release No. 21495 (November 16, 1984), 49 FR 46556 (November 27, 1984).

[3] As defined more fully in the Rule, direct participation programs are programs which provide for flow-through tax consequences to their investors such as limited partnerships or some investment contract securities. It is anticipated that such programs may include oil and gas, real estate, agricultural, cattle breeding, and equipment leasing programs.

[4] The Rule does not provide an exemption from the prohibition against the direct extension of credit by the broker-dealer, nor does it permit the broker-dealer to arrange for the extension of credit beyond the deferred payment itself.

will thus permit broker-dealers to participate in public offerings of securities of direct participation programs that provide for mandatory payments on a deferred basis,[5] provided that certain conditions are met. Specifically: (1) The securities must be registered under the Securities Act of 1933 ("1933 Act") or be offered exclusively on an intrastate basis in accordance with section 3(a)(11) of that Act, (2) the mandatory deferred payments must bear a reasonable relationship to the capital needs and program objectives describes in a business development plan, (3) a minimum of 50 percent of the purchase price of the program securities must be paid by the investor at the time the securities are sold; and (4) the total purchase price of a program security must be paid within three years in the case of specified property programs and two years in the case of non-specified property programs.

II. Background

Since 1972, Regulation T,[6] promulgated by the Board of Governors of the Federal Reserve System ("Board") under section 7 of the Exchange Act, and section 11(d)(1) of the Exchange Act,[7] have been interpreted to prohibit broker-dealers from participating in public offerings of securities of direct participation programs with mandatory installment or deferred payment features.[8] Sales of program securities with deferred payment features have been permissible, however, in private placements.[9] An effect of these prohibitions has been to force issuers to either eliminate deferred payments altogether in public offerings, use private placements for sales of interests in direct participation programs with mandatory installment payment features, or to make public offerings with voluntary installment payments.[10]

In 1972, shortly after the Board's staff indicated that Regulation T was applicable to public offerings of direct participation programs with installment features, the Commission's Real Estate Advisory Committee, composed of members of the real estate syndication industry and Commission staff, issued a report based upon a comprehensive review of the disclosure procedures and policy objectives in the area of real estate securities ("REAC Report"). Among the recommendations contained in the REAC Report was that the Commission use its rulemaking authority to exempt from the requirements of Regulation T interests in real estate limited partnerships where deferred payments "are made on a schedule based on anticipated need as is set forth in the registration statement." [11] More recently, in 1983, the National Association of Securities Dealers, Inc. ("NASD") petitioned the staff of the Board to provide relief in this area.[12] The NASD argued in its request that relief was appropriate since, among other things, the concerns which led Congress to adopt section 7(c) are not present in the context of deferred sales of direct participation programs. In addition, the NASD noted that regulatory oversight of the programs by the states, the NASD, and the federal government has increased substantially over the past decade.

The NASD suggested that sales of direct participation program interests on a deferred payment basis should be entirely exempt from the credit restrictions. Alternatively, the NASD suggested several conditions that could apply to such sales. After extensive consultation between the staff of the Board and the Commission's staff, it appeared that the most efficient way to expose the issue for public comment was for the Commission to propose a rule pursuant to its authority under section 3(a)(12) of the Exchange Act, which allows the Commission to define exempted securities.[13]

III. Determination To Adopt Rule 3a12–9

In response to the release proposing Rule 3a12–9, the Commission received letters from 125 commentators. The comment letters reflected a broad range of interests within the securities industry and were evenly divided in support of and opposition to adoption of the proposed Rule.[14] After evaluating the comment letters, the Commission has determined to adopt Rule 3a12–9, incorporating a number of changes in the Rule as a result of suggestions made in the comment letters. The Commission believes that permitting program interests to be sold on a deferred payment basis, so that payments by investors to a program can be coordinated to match the program's capital needs, will produce economic benefits to investors and program sponsors which justify adoption of the Rule. Nevertheless, the Commission also believes that the imposition of specific conditions in connection with sales of program interests with deferred payments is necessary to preserve investor protection.

Commentators noted that under the previous credit restrictions applied to public offerings of direct participation programs, investors were forced to make cash contributions at the outset of the program, even though a considerable portion of the funds might remain idle until used by the program, perhaps a significant period of time following termination of the offering. For example, where projects are completed over a

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[5] For some purposes a distinction may be drawn by state regulators between the terms "installment payments" and "deferred payments." The latter, which are intended to be encompassed by Rule 3a12–9, must bear a reasonable relationship to the program's cash needs and business objectives, and are not merely an optional method of financing the purchase of program interests over a period of time. Nevertheless, these two terms, along with the term "staged payments," may in some instances be used interchangeably for purposes of this release.

[6] 12 CFR Part 220.

[7] Section 11(d)(1) of the Exchange Act generally prohibits a broker-dealer who participates in a distribution of securities from extending or arranging for credit during the first 30 days following termination of the distribution.

[8] In March of 1972, the Board concluded that the sale by a broker-dealer of a publicly offered tax shelter program with installment features constitutes an "arranging" for the extension of credit in violation of Regulation T (12 CFR 220.124). Subsequently, the Board adopted an "economic penalty" test in determining whether the likelihood of an exercise of a warrant was so great as to make it equivalent to an installment purchase. Securities Credit Transactions Handbook section 5–560.31 (Board Ruling of October 30, 1973). *See also. Id. at* section 5–606.31 (Staff Op. September 30, 1983).

[9] In July of 1972, the Board's staff indicated that the prohibition against the use of installment payments under Regulation T set forth in its March interpretation related only to publicly offered programs which were not exempt from registration with the Commission. Securities Credit Transaction Handbook, section 5–551. In 1975, the Board amended Regulation T to except from the arranging prohibition those private offerings exempt from registration with the Commission pursuant to section 4(2) of the 1933 Act. *See*, 12 CFR 220.7(a). Because the prohibitions of section 11(d)(1) of the Exchange Act would have rendered an exemption for intrastate offerings ineffective, the staffs of the Board and the Commission concluded that an express exemption from Regulation T for intrastate offerings was inappropriate.

[10] Public offerings with deferred payment features have been conducted using so-called "toothless notes" which do not involve an economic penalty to the investors for failure to pay subsequent installations and therefore are permissible under Regulation T.

[11] *Report of the Real Estate Advisory Committee to the Securities and Exchange Commission*, at 65 (October 12, 1972.

[12] *See*, Letter dated April 26, 1983 to Robert S. Plotkin, Assistant Director of the Board, from Frank J. Wilson, Executive Vice President, NASD (publicly available in File No. S7–36–84).

[13] Section 3(a)(12) defines "exempted securities" to include such securities: "as the Commission may, by such rules and regulations as its deems consistent with the public interest and the protection of investors, either unconditionally or upon [specified terms and conditions or for stated periods, exempt from the operation of any [one] or more provisions of this title which by their terms do not apply to an "exempted security" or to "exempted securities."

[14] A summary of the comments prepared by the Commission's staff is available for public inspection and copying in File No. S7–36–84.

period of time in identifiable stages, the program may not need investor funds to make payments until work has been completed on a particular industry stage. In such cases, all the investor's money is at risk, while the program may hold unneeded funds providing the investor with either no return, or a return at a far lower rate than he or she might have received if allowed to make alternative investments until the program had an actual need for funds.

Commentators also pointed out that the Rule will allow program sponsors to access new sources of capital. Because programs with staged payments have only been available in private offerings, many investors, for whom investments in such programs would otherwise be suitable, were denied the opportunity to participate. Commentators argued that by permitting public offerings of direct participation programs with deferred payment features, the Rule will provide investors with new investment alternatives and, at the same time, facilitate the formation of programs with broader capital bases. The Commission believes that the Rule will reduce the current constraints on the formation of capital and eliminate the misallocation of investor resources without compromising investor protection or contravening the intent of Congress in enacting sections 7(c) and 11(d)(1).

The rationale behind the adoption of section 7 of the Exchange Act was to limit the amount of credit which might be devoted to speculation in the securities markets, to maintain the availability of credit for financing local commerce and industry, to prevent undue market volatility by exerting a positive, stabilizing effect on the market and, to protect investors from purchasing on too thin a margin. Section 11(d)(1), in turn, was enacted by Congress to prevent potential conflicts of interest which might arise where underwriters, who are both brokers and dealers, extend credit on new issues of securities.[15]

In deciding whether to adopt Rule 3a12–9, the Commission gave extensive consideration to the impact of the Rule in light of the Congressional philosophy underlying the credit restrictions. Since interests in direct participation programs are generally not traded on exchanges or actively traded in the over-the-counter market, they are considered to be illiquid instruments and therefore afford less opportunities for speculation and related abuses which Congress sought to prevent by enacting the credit restrictions. Although the Commission is aware that an active secondary market has developed for a few direct participation programs, it is not expected that programs with deferred payment features will be active traded. Moreover, limitations have been established in the Rule which are designed to preclude those direct participation programs with deferred payment features which are actively traded from taken advantage of the Rule's exemptive provisions.

Some commentators suggested that allowing direct participation programs with deferred payments to be sold through public offerings might lead to instances of broker-dealer overreaching. Many of the same commentators also forecast the possibility of widespread defaults on deferred payments by investors in public offerings who lacked the financial capacity to fulfill their commitments. By permitting programs with staged payments to be publicly offered, the Commission believes that Rule 3a12–9 will enhance investor protection.

Public offerings of direct participation program securities are subject to many regulatory standards imposed by the states and the NASD which are not directly applicable to most private offerings. For example, Appendix F to the NASD's Rules of Fair Practice[16] imposes additional regulation on public offerings direct participation programs in areas such as investor suitability, due diligence by members, the accuracy and adequacy of disclosure and the amount and form of underwriting compensation. In addition, separate state regulatory guidelines for the offering of direct participation programs in real estate, oil and gas, and equipment leasing have been adopted by the North American Securities Administrators Association, Inc. ("NASAA"), a voluntary organization comprised of state securities regulatory agencies. The NASAA guidelines, which are followed by many states and apply primarily to public offerings, establish standards regulating program sponsors, impose investor suitability requirements, and require that substantive features designed to protect investors are included in the partnership agreement.

In the Commission's view the provisions of the Rule, coupled with state laws, NASD regulations, and the antifraud provisions under the federal securities laws, are sufficient to protect investors against abusive sales practices. In this regard, broker-dealers are remined that Rule 15c2–5 under the Exchange Act requires that they make a suitability determination when arranging for the extension of credit in transactions, such as those under Rule 3a12–9, which are not subject to Regulation T.[17]

The Commission also notes that it has not been presented with any evidence that significant numbers of defaults have occurred in the private offerings of direct participation programs with deferred payment features which are currently being made. Indeed, the Commission understands that the number of defaults by investors in these offerings has been minimal. While the Commission recognizes that most purchases of program interests in private offerings have been accredited investors, the Commission has no basis upon which to conclude that other creditworthy investors, for whom the transactions are otherwise suitable, are more likely to default on their payments. In addition, provisions have been added to the Rule which require a substantial down payment and limit the duration of the pay-in period. These provisions will increase the incentive of the investor to fulfill his obligation to make additional payments and, at the same time, reduce the likelihood that unforeseen events will alter the economic attractiveness of the program or effect the investor's ability to make payments.[18]

Commentators also raised concerns that adoption of Rule 3a12–9 might cause sponsors to offer increased numbers of programs emphasizing tax benefits at the expense of the underlying economics of the programs' operations

[15] See, Securities Exchange Act Release No. 11220, 40 FR 6644 (February 13, 1975) (adopting Rule 3a12–5; 17 CFR 240.3a12–5). *See also, A Review and Evaluation of Federal Margin Regulations, A Study by the Staff of the Board of Governors of the Federal Reserve System* (December 1984).

[16] Appendix F to Art. III, Section 34, NASD Rules of Fair Practice.

[17] Rule 15c2–5 (17 CFR 240.15c2–5) states, among other things, that it shall constitute a "fraudulent, deceptive, or manipulative act or practice," as used in section 15(c)(2) of the Exchange Act, for a broker-dealer to arrange for credit in connection with the sale of any security unless, prior to the purchase, the broker-dealer obtains information concerning the financial situation and needs of the investor and reasonably determines that the entire transaction, including the loan arrangement, is suitable for the investor. Although this rule does not apply to transactions made in accordance with the provisions of Regulation T, it does not distinguish between public and private offerings. Accordingly, Rule 15c2–5's requirements are equally applicable to transactions which are not governed by Regulation T because they are either made pursuant to Rule 3a12–9 or because they are done in private offerings.

[18] Commentators indicated that it is currently the practice in many private offerings using installment payments to obtain insurance to protect the working capital of the program in the event of investor defaults. The Commission anticipates that similar practices will develop among publicly offered programs with staged payment features.

or perhaps encourage the promotion of abusive tax shelters. Because of this, they estimated that the Rule would adversely affect federal tax revenues. While the admininstration of federal tax policy is not within its jurisdiction, the Commission notes that the Internal Revenue Service has substantial weapons with which to monitor and combat abusive tax shelters.

In sum, the Commission believes that Rule 3a12–9 will provide a useful alternative for capital formation to sponsors that wish to provide for mandatory deferred payments in public offerings of direct participation programs. In addition, investors who previously were denied the opportunity to invest in such offerings will now have access to these programs. Finally, in the Commission's view, the Rule will eliminate the current misallocation of economic resources in a manner consistent with the protection of investors.

IV. Scope of Rule 3a12–9

A. General

As noted earlier, Rule 3a12–9 is designed to permit broker-dealers to participate in public offerings of securities with deferred payment features where the securities satisfy the provisions of the Rule. The Rule does not, however, require that all offerings with deferred payment features be offered on a public basis or that private offerings comply with its provisions. Instead, the Rule is intended to provide both investors and promoters with previously unavailable alternatives.

As adopted, the Rule contains a number of amendments which were made as a result of suggestions received from commentators. Specifically, in response to concerns raised by state regulations, along with members of the syndication industry, the Rule now contains several limitations designed to minimize the possibility of investor defaults and make the extension of credit under the Rule compatible with current regulations applied to margin securities under Regulation T of the Exchange Act. At the same time, however, the Commission has deleted requirements in the proposed Rule which commentators believed would impose additional costs or uncertainty on the part of program sponsors without a corresponding increase in investor protection.

B. Definition of Director Participation Program

As proposed, the Rule applied to direct participation program securities, which were defined as securities created pursuant to a contractual agreement between and among investors, that were not margin securities, and that provided direct flow through tax consequences to investors. The proposed Rule also specifically excluded from the defintion of a direct participation program certain forms of business organizations which might otherwise have fallen within the definition.

The definition of direct participation program as adopted in paragraph (b)(1) of the Rule has been broadened by eliminating the requirement that the program be created through contractual agreements between and among investors, and that tax consequences flow directly to investors. These changes were made, in part, to reflect commentator's observations that certain financing vehicles which fall within the spirit of the Rule, such as some investment contract securities, might be precluded from relying on the Rule if the definition of a direct participation program were adopted as proposed.[19]

Finally, the Commission recognizes that some program securities may have active secondary markets. These securities raise price volatility and supeculation concerns that are central to the policy underlying the Exchange Act's margin regulations. To ensure that actively traded securities are treated in a manner consistent with all other potentially marginable securities, the Commission is modifying the definition of a direct participation program to exclude securities that are listed on exchanges or quoted on NASDAQ during the pay-in period. In addition, the Rule will also not be applicable to securities that will otherwise be actively traded during the pay-in period as a result of the direct or indirect efforts of the issuer, underwriter, or other participants in the initial distribution to facilitate a trading market in the securities. Should active trading markets develop for direct participation program securities, generally, the Commission may re-evaluate the continued appropriateness of the Rule.

C. Deferred Payments Required Pursuant to a Business Development Plan

The proposed Rule contained a requirement that mandatory installment payments bear a direct relationship to the capital needs and program objectives as described in a business development plan disclosed in a registration statement filed with the Commission under the 1933 Act. A business development plan was defined as a specific plan of the program's anticipated economic development and the amount of future capital contributions to be requried at specified times or upon the occurrence of certain events during the life of the program. The Commission received a number of comments concerning the necessity of requiring a business development plan. Several commentators argued that the provision was unnecessary in light of current disclosure requirements for registered securities. In addition, members of the oil and gas industry were divided over whether their programs would be able to provide sufficient information about upcoming capital expenditures to fulfill such a requirement. Along the same lines, commentators questioned whether non-specified property programs, in general, would be able to meet such a standard.

In the Commission's view, disclosure of a business development plan will be a useful supplement to existing disclosure requirements for registered offerings. Since the fundamental purpose of the Rule is to allow sponsors to coordinate payments by investors with the capital needs of the program, the Commission believes that development of such a plan is necessary to establish the business reasons for offering securities with deferred payments. Although the Commission requested comment on the merits of imposing specific disclosure requirements, it has determined not to dictate the content of such disclosure, aside from the general description in the definition of a business development plan.[20]

[19] To the extent that other financing vehicles fall within the spirit of the Rule, but may not come directly within the definition of a direct participation program, the staff of the Commission's Division of Market Regulation will consider, on a case by case basis, requests for relief in the form of no-action or interpretive letters.

[20] One commentator suggested that the following information should be disclosed in the business development plan: (1) The investment and business objectives of the program; (2) the proposed investments and operations of the program; (3) the amount and timing of the financing for such investments and operations; (4) the relationship of such financing to the investment and business objectives of the program; (5) the relationship of installment payment provisions of the program, to the financing for the program, to the cash needs of the program, to the proposed investments and operations of the program; (6) any alternative or supplementary financing arranged by or available to the program to provide for future uncertainties (including possible inaccuracies in forecasts of financial needs and possible investor defaults); (7) the financial, contractual and tax consequences to the investor and to the program of defaults by investors in making mandatory installment payments. The Commission believes that this type of disclosure may be appropriate in connection with offerings of programs with staged payments.

The Commission has also decided to permit non-specified property programs to take advantage of the Rule's exemptive provisions.[21] Although such programs may not have determined specific property to be purchased with investor funds, it may be possible to reasonably fix the type, timing and necessity of future cash needs. Accordingly, the Commission believes that uniformly excluding non-specified programs from the Rule would not be appropriate.

As proposed, the Rule required that mandatory deferred payments bear a "direct" relationship to the capital needs of the program. Many commentators expressed concern that this requirement may prove difficult to apply. In light of these concerns, the Commission is modifying the requirement to state that installment payments from investors need only be "reasonably" related to the capital needs and business objectives of the program. Nevertheless, the Commission wishes to make clear that programs relying on the Rule must coordinate payments so that they bear a reasonable relationship to substantive program events or capital needs. Programs which intend at the outset of the offering to factor or otherwise assign investor notes in order to raise capital to purchase property or meet program objectives prior to receipt of the deferred payments, will not meet this test and cannot rely on the Rule. The Commission recognizes, however, that investor notes are program assets and it does not intend to unreasonably encumber their use by programs relying on this Rule. Accordingly, investor notes may be used as collateral to secure program debt.

D. Registration of Securities

The proposed Rule would have required that program securities be registered pursuant to the 1933 Act and that the securities remain registered under section 12(g) of the Exchange Act until the total purchase price of the security was paid. Since public intrastate offerings of securities need not be registered with the Commission by virtue of section 3(a)(11) of the 1933 Act,[22] the Commission requested comment on the merits of exempting intrastate offerings from these requirements. As adopted, the Rule continues to require registration under the 1933 Act, with the exception of programs making unregistered public offerings in reliance upon section 3(a)(11) of the 1933 Act. Those programs offered in reliance on section 3(a)(11) will also be able to utilize the Rule provided they meet its other requirements and disclosure of the business development plan is made in the relevant state filing and provided to investors. In deciding to extend the Rule to public intrastate offerings, the Commission weighed heavily the fact that many states' securities regulations require substantially the same disclosure as required on Form S-1 under the 1933 Act and that public intrastate offerings would remain subject to NASD and state guidelines as well as relevant provisions of the federal securities laws.[23]

As a result of comments received, the Commission is eliminating the requirement that all programs utilizing the exemption remain subject to the reporting requirements of section 12(g) of the Exchange Act until the total purchase price of the securities is paid. Commentators suggested that compelling issuers to register under section 12(g), who might not otherwise be required to do so, would increase expenses on the part of some smaller programs and be of little or no additional benefit to investors. They also noted that those offerings registered with the Commission would generally be subject to the annual reporting requirements under section 15(d) of the Exchange Act during the first year of operation. In light of these arguments, as well as the imposition of maximum pay-in periods, and the understanding that annual or periodic disclosure is currently required of publicly offered programs under many states' securities laws, the Commission has decided to remove the provision that programs remain subject to the reporting requirements under Section 12(g) as a prerequisite for qualification under the Rule. Nevertheless, issuers relying on the Rules should be aware that they are not relieved of the responsibility for complying with reporting obligations that may otherwise exist.

E. Maximum Pay-In Period; Required Down Payment

In the proposing release, the Commission requested comment on whether the Rule should specify an outside time limit by which installation payments must be made. In addition, the Commission inquired whether different maximum pay-in periods should be imposed on specified and non-specified property programs. The proposing release noted that the NASD had previously suggested that the total purchase price of a program interest might be required to be discharged in a period of three years from the date the investor is admitted as a limited partner in a non-specified property program or five years in a specified property program.

The Commission believes that investor protection will be increased, while continuing to provide issuers and investors with substantial flexibility, by limiting the amount of time over which the deferred payments must be made. As adopted, the Rule provides that the maximum period over which deferred payments may be made is two years for non-specified property programs and three years for specified property programs. Although commentators suggested a variety of maximum pay-in periods, the Commission anticipates that the time periods incorporated in the Rule should satisfy the business needs of most programs and at the same time reduce the possibility that either the investor or program will experience financial adversities during the pay-in period. A distinction has also been drawn between specified and non-specified programs, in part, to reflect the greater economic risks inherent in non-specified programs. Further, time periods will be measured from the earlier of the completion of the offering or one year from the effective date of the offering, rather than the date the investor is included in the program as suggested in the proposing release.[24] This latter modification was made to avoid administrative problems associated with multiple admission dates for investors which might have

[21] For purposes of the Rule, a specified property program is defined as a program in which at the time of securities registration, 75 percent of the amount of money available for investment is committed to specific program expenditures. A non-specified property program would be one in which less than 75 percent of the money available for investment has been so committed. Examples of specifically identifiable program expenditures would include the purchase of a particular parcel of real property or type of computer equipment. Specifically identifiable program expenditures would not include expenditures committed to a broad category of equipment such as "transportation equipment," or to other than specific parcels of real property.

[22] Rule 147 under the 1933 Act (17 CFR 230.147) provides a non-exclusive "safe harbor" from securities registration for intrastate offerings that meet its requirements.

[23] Outside of the context of the Rule, the Commission continues to believe that section 11(d)(1) prohibits a person who is both a broker and a dealer from extending or arranging for the extension of credit in the distribution of a new issue of securities offered on an intrastate basis.

[24] The effective date of the offering for purposes of the Rule will generally be the date the registration statement is declared effective by the Commission. Where offerings are conducted in reliance upon the intrastate exemption under section 3(a)(11) of the 1933 Act, the effective date will be the date upon which the offering is approved by state securities administrators.

existed under the proposed method for calculating time periods.

In addition to imposing maximum time periods over which installment payments must be made, the Rule requires a minimum down payment of 50 percent of the purchase price of the program security. By requiring a substantial down payment, the Commission expects to alleviate many of the concerns raised by commentators that excessive leveraging of program securities might result in customer sales practice abuses and substantial defaults.[25] It should be noted, however, that the Rule now requires payment of the initial portion of the purchase price to be made at the time of sale, rather than over the course of twelve months as suggested by the NASD.

The Commission recognizes that the availability of staged payments for public offerings of direct participation programs may have a substantial impact on the structure and investor population of those markets. Therefore, the Commission believes that initially a cautious approach including limited pay-in periods and minimum down payments is advisable. After the Commission has had an opportunity to monitor the effects of the Rule, it anticipates reevaluating, in conjunction with state securities regulators, the limitations presently contained in the Rule.

V. Contingency Offerings

Since securities of direct participation programs are frequently offered on an "all or none" or "part or none" basis, the Commission solicited comments on the application of Rules 10b–9 and 15c2–4 of the Exchange Act [26] to public offerings made in reliance on rule 3a12–9. Rule 10b–9 requires specificity in the terms of contingency offerings. In other words, a specified amount of securities ("specified sales level") must be sold at a specified price within a specified time, and the total amount due to the seller (*i.e.*, the issuer) must be received by it by a specified date. Moreover, Rule 10b–9 also requires that, if the contingencies are not satisfied fully by the specified date, "all or a specified amount" of the consideration paid must be promptly refunded to the purchaser. Rule 15c2–4 addresses the handling of investor funds by broker-dealers in contingency offerings and provides that, prior to the satisfaction of all contingencies, any consideration received by broker-dealers from investors must either be promptly deposited by the broker-dealer in a separate bank account as agent or trustee for the persons who have the beneficial interests therein, or promptly transmitted to a bank which has agreed in writing to hold all such consideration in escrow for the persons who have the beneficial interests therein.

After considering the views of the commentators, the Commission believes that a security offered on an "all or none" or "part or none" basis pursuant to Rule 3a12–9 is "sold" for purposes of Rule 10b–9 when the issure or a broker-dealer participating in the offering receives the consideration specified by the terms of the offering. The specified consideration would consist of the 50 percent down payment and the documentation reflecting the contractual obligation of the investor to make mandatory installment payments. Rule 10b–9 would be satisfied, and the consideration may be released to the issuer, only where: (1) The specified sales level is achieved; (2) with respect to the sale of each security counted towards the specified sales level, the 50 percent down payment is fully paid; [27] and (3) the required documentation reflecting the installment payment obligation comports with the requirements of the offering material. Any consideration received by a broker-dealer in a Rule 3a12–9 offering prior to satisfaction of the contingencies must be deposited or transmitted in compliance with Rule 15c2–4.

VI. Coordination With State Securities Regulators

As noted earlier, the Commission's decision to adopt Rule 3a12–9 at this time is based, in part, upon the increased quality of state securities regulations which will be applicable to many of the offerings able to utilize the Rule. In drafting the final version of the Rule, the Commission has sought to minimize some of the conflicts between the Rule and the NASAA guidelines for certain direct participation programs which are applied by many states. However, the Commission recognizes that conflicts do exist.

The Commission wishes to emphasize that Rule 3a12–9 is an exemptive rule under the federal securities laws only and is not intended to pre-empt state securities laws. Accordingly, those securities which qualify under the Rule to be deemed exempted securities for purposes of the arranging for credit provisions of sections 7(c) and 11(d)(1) of the Exchange Act must also comply with applicable state securities laws. The Commission is hopeful that the additional investor safeguards which have been incorporated in the Rule will facilitate complementary amendments to present state securities regulations. Staff of the Commission's Division of Market Regulation will be working with members of NASAA in an effort to resolve conflicts.

VII. Certain Findings, Effective Date and Statutory Basis

Section 23(a)(2) of the Exchange Act [28] requires the Commission, in adopting rules under that Act, to consider the anticompetitive effect of such rules, if any, and to balance any impact against the regulatory benefits gained in terms of furthering the purposes of the Exchange Act. The Commission has considered proposed Rule 3a12–9 in light of the standards cited in section 23(a)(2) and believes that adoption of the Rule will not impose any burden on competition not necessary or appropriate in furtherance of the Act. Indeed, the Commission believes that the Rule will enhance competition by increasing issuers' flexibility in constructing and offering direct participation programs to suitable investors.

Pursuant to the Administrative Procedure Act, 5 U.S.C. 553(b) interested persons were given an opportunity to submit written views on proposed Rule 3a12–9. After consideration of the relevant matters, the Rule is being adopted substantially as proposed, but with certain changes made in response to suggestions of commentators. In response to comments received, the requirement in the proposed Rule that all securities issued in reliance on the Rule remain subject to the reporting requirements of section 12(g) of the Exchange Act has been eliminated. In addition, the Rule's coverage has been expanded to include securities offered on an intrastate basis which are registered with state securities administrators. Provisions have also been added to the Rule requiring a minimum down payment and limiting the amount of time over which deferred payments may be made.

Since Rule 3a12–9 is exemptive in nature, pursuant to section 553(d) of the Administrative Procedure Act, [5 U.S.C. 553(d)] it may become effective immediately upon publication in the **Federal Register.** However, in recognition of the fact that state securities administrators may wish

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[25] This portion of the Rule is intended to be in parity with the margin requirements under Regulation T. If those requirements change, the Commission may wish to reexamine the minimum down payment requirement of the Rule in light of those changes.

[26] 17 CFR 240.10b–9 and 240.15c2–4.

[27] It should be noted that the down payment would be considered to be fully paid only upon the receipt of cleared funds.

[28] 15 U.S.C. 78w(a)(2).

some time to study the Rule, the Commission decided to delay its effectiveness for 30 days following publication in the **Federal Register.**

VIII. Summary of Final Regulatory Flexibility Analysis

The Commission has prepared a Final Regulatory Flexibility Analysis for Rule 3a12-9 in accordance with 5 U.S.C. 603. The Analysis notes that Rule 3a12-9 is designed to allow programs, which do not need all investors funds at the outset, to match investor payments for program securities sold in public offerings with the actual capital needs of the program. Programs with staged payment features are currently permitted only in private offerings. The Analysis indicates that Rule 3a12-9 will provide promoters with alternative means of raising capital and will give investors new investment choices, without compromising investor protection. No commentators specifically referred to the Initial Regulatory Flexibility Analysis. However, the Analysis notes the Commission has deleted certain requirements in the proposed Rule which commentators believed would impose additional costs or uncertainty on the part of program sponsors without a corresponding increase in investor protection.

A copy of the Final Regulatory Flexibility Analysis may be obtained by contacting Edward L. Pittman, Esq., Division of Market Regulation, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549 (202) 272-2848.

IX. Statutory Basis

The Securities and Exchange Commission, acting pursuant to the Exchange Act, 15 U.S.C. 78a *et. seq.*, and particularly sections 3(a)(12), 7(c), 11(d)(1) and 23 [15 U.S.C. 78c(a)(12), 78g, 78k and 78w], hereby amends Chapter II, Title 17 of the Code of Federal Regulations by adding § 240.3a12-9 thereto.

List of Subjects in 17 CFR Part 240

Brokers, Credit, Securities.

Text of Rule 3a12-9

Chapter II, Title 17 of the Code of Federal Regulations is amended as follows:

PART 240—GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE ACT OF 1934

1. The authority citation for Part 240 is amended by adding the following citation: (Citation before * * * indicates general rulemaking authority)

Authority: Sec. 23, 48 Stat. 901, as amended (15 U.S.C. 78w). * * * § 240.3a12-9 also issued under secs. 3(a)(12), 7(c), 11(d)(1), 15 U.S.C. 78c(a)(12), 78g(c), 78k(d)(1)).

2. Section 240.3a12-9 is added to read as follows:

§ 240.3a12-9 Exemption of certain direct participation program securities from the arranging provisions of sections 7(c) and 11(d)(1).

(a) Direct participation program securities sold on a basis whereby the purchase price is paid to the issuer in one or more mandatory deferred payments shall be deemed to be exempted securities for purposes of the arranging provisions of sections 7(c) and 11(d)(1) of the Act, provided that:

(1) The securities are registered under the Securities Act of 1933 or are sold or offered exclusively on an intrastate basis in reliance upon section 3(a)(11) of that Act;

(2) The mandatory deferred payments bear a reasonable relationship to the capital needs and program objectives described in a business development plan disclosed to investors in a registration statement filed with the Commission under the Securities Act of 1933 or, where no registration statement is required to be filed with the Commission, as part of a statement filed with the relevant state securities administrator;

(3) Not less than 50 percent of the purchase price of the direct participation program security is paid by the investor at the time of sale;

(4) The total purchase price of the direct participation program security is due within three years in specified property programs or two years in non-specified property programs. Such pay-in periods are to be measured from the earlier of the completion of the offering or one year following the effective date of the offering.

(b) For purposes of this Rule:

(1) "Direct participation program" shall mean a program financed through the sale of securities, other than securities that are listed on an exchange, quoted on NASDAQ, or will otherwise be actively traded during the pay-in period as a result of efforts by the issuer, underwriter, or other participants in the initial distribution of such securities, that provides for flow-through tax consequences to its investors; *Provided, however,* that the term "direct participation program" does not include real estate investment trusts, Subchapter S corporate offerings, tax qualified pension and profit sharing plans under sections 401 and 403(a) of the Internal Revenue Code ("Code"), tax shelter annuities under section 403(b) of the Code, individual retirement plans under section 408 of the Code, and any issuer, including a separate account, that is registered under the Investment Company Act of 1940.

(2) "Business development plan" shall mean a specific plan describing the program's anticipated economic development and the amounts of future capital contributions, in the form of mandatory deferred payments, to be required at specified times or upon the occurrence of certain events.

(3) "Specified property program" shall mean a direct participation program in which, at the date of effectiveness, more than 75 percent of the net proceeds from the sale of program securities are committed to specific purchases or expenditures. "Non-specified property program" shall mean any other direct participation program.

By the Commission.

Dated: March 7, 1986.

John Wheeler,

Secretary.

[FR Doc. 86-5623 Filed 3-13-86; 8:45 am]

BILLING CODE 8010-01-M

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17 CFR Part 240

[Release No. 34-22975; File No. S7-40-85]

Short Sales of Securities

AGENCY: Securities and Exchange Commission.

ACTION: Adoption of final rule amendments.

SUMMARY: In connection with extending unlisted trading privileges to certain over-the-counter stocks and permitting certain listed securities to be concurrently designated National Market System Securities, the Commission is adopting amendments to its short sale rule that exclude from application of the rule transactions in National Market System-Designated Securities that are traded on an exchange on a listed or unlisted trading privileges basis.

EFFECTIVE DATE: April 21, 1986.

FOR FURTHER INFORMATION CONTACT: Andrew E. Feldman, Esq., (202) 272-2414, Room 5205, Division of Market Regulation, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549.

SUPPLEMENTARY INFORMATION:

I. Summary

Rule 10a-1 ("short sale rule" or "Rule")[1] under the Securities Exchange

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[1] 17 CFR 240.10a-1.

Act of 1934 ("Act")[2] prohibits execution of short sales under certain conditions. The Rule applies, among other things, to securities registered on, or admitted to unlisted trading privileges ("UTP") on, a national securities exchange for which last sale information is reported pursuant to an "effective transaction reporting plan."[3] As such, Rule 10a-1 applies to listed securities traded on an exchange or in the third market[4] and reported through the consolidated transaction reporting system, but not to purely over-the-counter ("OTC") securities.

On September 16, 1985, the Commission issued two releases that, without further action, would subject transactions in two groups of OTC securities designated as National Market System Securities ("NMS Securities" or "NMS Designated Securities")[5] to the Rule for the first time. First, the Commission announced the terms and conditions for exchanges to commence trading NMS Securities on a UTP basis.[6] Second, the Commission adopted amendments to the NMS Designated Securities Rule to allow listed securities that are not reported in the consolidated transaction reporting system to be designated as NMS Securities.[7] Because last sale information on NMS Securities is reported pursuant to an "effective transaction reporting plan," transactions in NMS Designated Securities that are traded on an exchange on the basis of either UTP or a concurrent listing automatically would be subject to short sale regulation, whether those transactions occur on an exchange or OTC.

The Commission, however, has not made a determination on the extent to which Rule 10a-1 should apply to NMS Designated Securities. On September 16, 1985, therefore, the Commission proposed amendments to Rule 10a-1 to exclude transactions in NMS Designated Securities from the Rule until the question of OTC short sale regulation is resolved.[8] The Commission today adopts the amendments to the short sale rule as proposed.

II. Background

Section 10(a) of the Act grants the Commission authority to regulate short sales in securities.[9] Consistent with that authority, the Commission in 1938 adopted Rule 10a-1 under the Act,[10] which is generally designed to prohibit short selling from accelerating a declining market.[11] It applies, among other things, to securities registered on or admitted to UTP on a national securities exchange for which last sale information is reported pursuant to an "effective transaction reporting plant."[12] The short sale rule uses a tick test that compares the price of a proposed short sale to immediately preceding transactions to determine its permissibility: short sales may be effected only on a plus tick (*i.e.*, at a price above the price at which the immediately preceding last sale was effected) or a zero-plus tick (*i.e.*, at a price equal to the last sale if the last preceding transaction at a different price was at a lower price). The base price is determined by reference to the last sale either in the consolidated transaction reporting system or in a particular marketplace.[13]

Prior to 1975, Rule 10a-1 covered short sales in reported listed securities effected only on exchanges. OTC trading in reported securities was not subject to any short selling restrictions, in part because last sale reports were not available for OTC transactions.[14] In connection with the implementation of the CTA Plan in 1974, the Commission extended Rule 10a-1 to third market transactions in listed securities included in the consolidated system.[15]

In adopting the NMS Securities Rule and thereby extending last sale reporting to those solely OTC-traded securities designated as NMS Securities, the Commission specifically sought comment on whether short sale limitations should be extended to NMS

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[2] 15 U.S.C. 78a *et seq.*

[3] The Commission's transaction reporting rule, Rule 11Aa3-1 under the Act, defines an "effective transaction reporting plan" as a plan approved by the Commission for collecting, processing, and disseminating transaction reports in reported securities. 17 CFR 240.11Aa3-1(a)(3). *See also* 17 CFR 240.11Aa3-1(a)(4)-(6). Transaction reports for listed securities from all markets are collected and disseminated in the "consolidated transaction reporting system" pursuant to such a plan administered by the Consolidated Tape Association ("CTA"). The CTA members are the New York ("NYSE"), American ("Amex"), Boston, Cincinnati, Midwest, Pacific, and Philadelphia Stock Exchanges, and the National Association of Securities Dealers ("NASD"). Transactions is securities either listed on the NYSE and Amex, or listed on a regional stock exchange that substantially meet the NYSE or Amex listing standards, are reported to the CTA.

[4] The third market is a term used to describe over-the-counter transactions in listed securities.

[5] Rule 11Aa2-1 under the Act ("NMS Securities Rule") sets forth the criteria and procedures by which certain OTC securities are designated as NMS Securities. 17 CFR 240.11Aa2-1. *See* Securities Exchange Act Release No. 21583 (December 18, 1984), 50 FR 730 ("NMS Amendments Release"); Securities Exchange Act Release No. 17549 (February 17, 1981), 46 FR 13992 ("NMS Adoption Release"). The primary effect of designation as an NMS Security is that the security is subject to last sale reporting requirements similar to those applicable to exchange traded securities. Transaction reports are collected and disseminated through the NASD's NASDAQ system pursuant to a transaction reporting plan administered by the NASD. These securities and listed securities included in the consolidated transaction reporting system are "reported securities". *See* 17 CFR 240.11Aa3-1(a)(4).

[6] Securities Exchange Act Release No. 22412 (September 16, 1985), 50 FR 38640 ("OTC/UTP Release").

[7] Securities Exchange Act Release No. 22413 (September 16, 1985), 50 FR 38515 ("OTC/Listed NMS Securities Release").

[8] *See* Securities Exchange Act Release No. 22414 (September 16, 1985) 50 FR 38671 ("Rule 10a-1 Exclusion Proposal Release"). The Commission has published a release soliciting comment on whether to extend short sale regulation to NMS Securities. *See* Securities Exchange Act Release No. 22127 (June 21, 1985). 50 FR 26584 ("NMS Concept Release"). *See also* Securities Exchange Act Release No. 22507 (October 4, 1985), 50 FR 41907.

[9] 15 U.S.C. 78j.

[10] *See* Securities Exchange Act Release No. 1548 (January 24, 1938) ("Rule 10a-1 Adoption Release"). In addition to Rule 10a-1, the Commission adopted Rule 3b-3 under the Act, which defines the term "short sale" as any sale of a security which the seller does not own or any sale which is consummated by the delivery of a security borrowed by, or for the account of, the seller. *See id.*

[11] The objectives of Rule 10a-1 were discussed in the *Special Study of Securities Markets*, which stated that short sale regulation should:

(1) Allow relatively unrestricted short selling in an advancing market;

(2) Prevent short selling at successively lower prices, thus eliminating short selling as a tool for driving the market down;

(3) Prevent short sellers from accelerating a declining market by exhausting all remaining bids at one price level, causing successively lower prices to be established by long sellers.

Report of Special Study of Securities Markets of the Securities and Exchange Commission (1963), *reprinted in* H.R. Doc. No. 95, 88th Cong., 1st Sess. 251.

[12] *See supra* note 3.

[13] 17 CFR 240.10a-1(a)(1). The "equalizing exemption" to the Rule, however, allows a market maker (*i.e.*, an exchange specialist, registered exchange market maker, or third market maker) to effect short sales for his own account at a price equal to the last sale price reported in the consolidated system, or to the market makers' most recent published offer, if that offer when published equaled the last sale previously reported. Nonetheless, any exchange by rule may prohibit its registered specialists and registered exchange market makers from availing themselves of this exemption. *See* 17 CFR 240.10a-1(e)(5). NYSE rules, for example, prohibit NYSE specialists from selling short specialty stocks in reliance upon the equalizing exemption. *See* NYSE Rule 440B.

[14] *See* Securities Exchange Act Release No. 11468 (June 12, 1975), 40 FR 25442, 25443 ("1975 Rule 10a-1 Amendments Release"). In the absence of publicity concerning OTC short sales (such as that afforded by the consolidated transaction reporting system), there appeared to be little reasons to fear that such sales would have a manipulative or destabilizing impact on the markets. *Id.* at 25443.

[15] The Commission concluded that the publicity provided by the consolidated system for OTC transactions in reported listed securities justified the application of Rule 10a-1. *See* 1975 Rule 10a-1 Amendments Release, *supra* note 14, at 25443.

Designated Securities.[16] Recognizing that last sale reporting has become an established part of the OTC market, the Commission in a recent release [17] again solicited comment on whether and how short sales in OTC Securities designated as NMS Securities should be regulated.[18]

While that request for comment was still outstanding, the Commission announced the terms and conditions for exchanges to commence trading NMS Designated Securities on a UTP basis [19] and, at the same time, adopted amendments to the NMS Securities Rule to allow non-reported listed securities to be designated as NMS Securities.[20] Recognizing that exchange listing of or UTP in NMS Designated Securities could bring those NMS Designated Securities within the short sale rule for the first time, the Commission solicited comment on whether, in view of its ongoing consideration of NMS Designated Securities short sale regulation, it should suspend the application of Rule 10a–1 to the limited group of NMS Designated Securities subject to concurrent exchange trading.[21]

III. Comments

The Commission received three comments on the proposed amendments, two in favor and one opposed. The National Association of Securities Dealers, Inc. ("NASD") and PaineWebber Group Inc. ("PaineWebber") supported the proposed amendments to the Rule.[22] PaineWebber stated that the Commission should address short sale regulation of NMS Designated Securities on an omnibus basis and, together with the NASD, asserted that subjecting certain NMS Designated Securities to short sale regulation because an exchange sought UTP in those securities would be both inappropriate and create confusion in the market. The NASD also contended that NMS Designated Securities traded on an exchange on a listed or UTP basis apparently did not need short sale regulation because competition between multiple market makers and exchange specialists would insure deep and liquid markets that were not readily susceptible to manipulation. The NASD finally noted that trading in these securities without the application of the Rule would provide valuable empirical data on how the markets operate in a UTP environment without short sale constraints.

The Philadelphia Stock Exchange ("Phlx") opposed the proposed amendments to Rule 10a–1.[23] The Phlx said that the short sale rule should apply to all transactions in exchange-traded NMS Designated Securities whether such transactions occur on an exchange or in the OTC market.[24] The Phlx asserted that Rule 10a–1 has prevented manipulation in listed markets, and would be particularly valuable in an OTC/UTP context because of the lack of intermarket linkages. However, the Phlx stated that, if the Commission decided to adopt the amendments to Rule 10a–1 as proposed, both OTC market makers and exchange specialists in NMS Designated Securities traded on an exchange on a listed or a UTP basis should be exempted from short sale regulation.

IV. Discussion

The Commission has sought public comment on the appropriateness of extending Rule 10a–1 generally to NMS Designated Securities. The Commission has separately proposed these narrow amendments to the short sale rule in recognition that, unless Rule 10a–1 was amended, concurrent exchange trading and NMS designation would result in certain NMS Designated Securities falling under the Rule for the first time. Specifically, once trading in these securities begins in multiple markets pursuant to an "effective transaction reporting plan," persons engaging in transactions in such NMS Designated Securities either on an exchange or OTC would have to comply with short selling regulations.

After considering the comments, the Commission is adopting the amendments to Rule 10a–1 as proposed. The Commission believes that short sale regulation with respect to NMS Designated Securities should be addressed on a generalized basis and not through the automatic application of the Rule as a result of allowing exchanges to trade certain NMS Designated Securities. As discussed previously, the Commission is still studying the broader question whether short sale regulation should apply to some or all NMS Designated Securities. Applying the short sale rule to NMS Designated Securities traded by exchanges would potentially be confusing because, at least initially, only a small number of NMS Designated Securities would be subject to these restrictions.[25] Moreover, these securities would be subject to the Rule even if there was little or no actual exchange trading in these securities.[26]

The amendments to Rule 10a–1 are narrow in scope, and apply only to transactions by OTC market makers and exchange specialists in those NMS Designated Securities that are subject to either UTP or a concurrent exchange listing. The amendments apply to both the exchange and OTC markets so that the existing regulatory treatment of short sales in competing markets will be maintained.

V. Effects on Competition and Regulatory Flexibility Act Considerations

Section 23(a)(2) of the Act [27] requires the Commission, in adopting rules under the Act, to consider the anticompetitive effects of such rules, if any, and to balance any anticompetitive impact against the regulatory benefits gained in terms of furthering the purposes of the Act. The Commission has examined the

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[16] NMS Adoption Release, *supra* note 5, at 14001–02. In response to that solicitation, the NASD stated that "short selling regulations prior to and during a distribution of NMS Securities would be appropriate but that it is not necessary, at this time, to impose across-the-board short sale regulations on transactions in NMS Securities." Letter from S. William Broka, Secretary, NASD, to George A. Fitzsimmons, Secretary, SEC (July 31, 1981).

[17] *See* NMS Concept Release, supra note 8, at 26587. There were over 1900 NMS Securities as of June 1985, and 2182 as of December 31, 1985.

[18] The extended comment period on this release expired on December 30, 1985. *See* Securities Exchange Act Release No. 22507 (October 4, 1985), 50 FR 41907. The Commission is analyzing the views of commentators.

[19] *See* OTC/UTP Release, *supra* note 6.

[20] *See* OTC/Listed NMS Securities Release, *supra* note 7.

[21] *See* Rule 10a–1 Exculsion Proposal Release, *supra* note 8, at 38672–73.

[22] *See* Letter from Sam Scott Miller, Vice President, General Counsel, and Secretary, PaineWebber, to John Wheeler, Secretary, SEC (January 9, 1986); *See* Letter from Frank J. Wilson, Executive Vice President and General Counsel, NASD, to John Wheeler, Secretary, SEC (October 31, 1985).

[23] *See* Letter from Michael A. Finnegan, Senior Vice President, Phlx, to John Wheeler, Secretary, SEC (November 8, 1985).

[24] The Phlx contended that OTC market makers in NMS Securities subject to UTP, like exchange specialists, should be permitted to avail themselves of the equalizing exemption of Rule 10a–1. For a discussion of the equalizing exemption, see *supra* note 13.

[25] Under the UTP pilot program that will last for one year following the commencement of OTC/UTP trading, each exchange will be able to trade up to 25 NMS Securities on a UTP basis. *See* OTC/UTP Release *supra* note 6, at 38646.

[26] The Commission notes that there are a small number of NMS Securities that currently are traded on an exchange on a listed or UTP basis. The vast preponderance of trading in these issues has occurred in the OTC market rather than on the exchanges. *See Id.*

[27] 15 U.S.C. 78w(a)(2).

proposed amendments to Rule 10a-1 in light of the standards set forth in section 23(a) and concludes that adoption of these amendments would not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. The Commission notes that the proposed amendments would exempt both exchange and OTC market participants form the short sale prohibitions that would otherwise govern transactions in NMS Designated Securities that are traded on an exchange on a listed or UTP basis. The amendments would continue in effect the differing treatment of short sales currently in place for securities that are primarily exchange traded and those that are not listed on an exchange. The Commission does not believe, however, that the narrow amendments adopted here would impose any new or different burdens on competition on competing markets or market participants. The Commission, therefore, believes that the proposed amendments would not impose any significant competitive burdens, and that the amendments are consistent with the objectives of section 11A of the Act.[28]

The Commission has prepared a Final Regulatory Flexibility Analysis ("FRFA"), pursuant to the requirements of the Regulatory Flexibility Act,[29] regarding the amendments to Rule 10a-1. The FRFA indicates that the amendments would exempt from Rule 10a-1 persons engaging in transactions in NMS Designated Securities subject to UTP or to a concurrent exchange listing. The FRFA notes that the principal effect of this exemption would be to relieve exchange specialists, OTC market makers, and other market participants from obligations governing short selling to which they otherwise would be subject. The FRFA states that, because the amendments would exempt persons from regulation, the proposal would not appear to impose significant costs upon those persons affected. The FRFA notes that no commentators specifically referred to the Initial Regulatory Flexibility Analysis in commenting on the amendments or indicated that the amendments might impose any other costs.

A copy of the FRFA may be obtained by contacting Andrew E. Feldman, Esq., (202) 272-2414, Division of Market Regulation, Securities and Exchange Commission, 450 5th Street, NW., Washington, DC 20549.

[28] *See, e.g.,* Sections 11A(1)(c)(ii) and 11A(c)(1)(F).

[29] 5 U.S.C. 601 et seq.

List of Subjects in 17 CFR Part 240

Reporting and recordkeeping requirements, Securities.

VI. Statutory Basis and Text of the Amendments

Pursuant to the Securities Exchange Act of 1934 and particularly sections 10(a) and 23(a) thereof, 15 U.S.C. 78j and 78w(a), the Commission is amending § 240.10a-1 in Chapter II to Title 17 of the Code of Federal Regulations.

Text of Amendments to Rule 10a-1

Chapter II, Title 17 of the Code of Federal Regulations is Amended as follows:

PART 240—GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE ACT OF 1934

1. The authority citation for Part 240 continues to read as follows:

Authority: Secs. 2, 3, 6, 9, 10, 15, 17 and 23, Pub. L. 78-291, 48 Stat. 881, 882, 885, 889, 891, 895, 897 and 901, as amended by secs. 2, 3, 4, 11, 14 and 18, Pub. L. 94-29, 89 Stat. 97, 104, 121, 137 and 155 (15 U.S.C. 78b, 78c, 78f, 78i, 78j, 78o, 78q, and 78w); sec. 15A, as added by sec. 1, Pub. L. 75-719, 52 Stat. 1070, as amended by sec. 12, Pub. L. 94-29, 89 Stat. 127 (15 U.S.C. 78o-3); sec. 11A as added by sec. 7, Pub. L. 94-29, 89 Stat. 111 (15 U.S.C. 78k-1); 15 U.S.C. 78a *et seq.*, and particularly secs. 2, 3, 10(a), 10(b), 15(c), and 23(a), 15 U.S.C. 78b, 78c, 78i(a)(6), 78j(a), 78j(b), 78o(c), and 78w(a).

2. Section 240.10a-1 is amended by redesignating (a)(1) as (a)(1)(i) and change the existing internal designations to (A) and (B), and adding new (a)(1)(ii) as follows:

§ 240.10a-1 Short sales.

(a) * * *

(1) * * *

(ii) The provisions of paragraph (a)(1)(i) hereof shall not apply to transactions by any person in National Market System Securities as defined in § 240.11Aa2-1 (Rule 11Aa2-1 under the Act).

By the Commission.

John Wheeler,

Secretary.

March 6, 1986.

[FR Doc. 86-5676 Filed 3-13-86-8:45 am]

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DEPARTMENT OF ENERGY

Federal Energy Regulatory Commission

18 CFR Part 389

[Docket No. RM86-6-000]

Construction Work in Progress; Anticompetitive Implications

Issued March 10, 1986.

AGENCY: Federal Energy Regulatory Commission, DOE.

ACTION: Final rule; notice of OMB control number.

SUMMARY: On February 27, 1986, the Federal Energy Regulatory Commission issued an interim rule in Docket No. RM86-6-000, 51 FR 7774 (March 6, 1986) establishing interim procedures to be followed concerning requests for construction work in progress in rate base. This notice states the OMB control number for § 35.26 promulgated in this docket.

EFFECTIVE DATE: March 10, 1986.

FOR FURTHER INFORMATION CONTACT: Ellen Brown, Federal Energy Regulatory Commission, 825 North Capitol Street, NE., Washington, DC 20426 (202) 357-8272.

SUPPLEMENTARY INFORMATION: The Paperwork Reduction Act, 44 U.S.C. 3501-3520 (1982), and the Office of Management and Budget's (OMB) Regulations, 5 CFR Part 1320 (1985), require that OMB approve certain information collection requirements imposed by agency rule. On March 5, 1986, OMB approved the information collection requirements of § 35.26 which were adopted pursuant to Order No. 448, 51 FR 7774 (March 6, 1986) and issued Control Number 19020096 for that section.

Accordingly, Part 389, Chapter I, Title 18, *Code of Federal Regulations*, is amended as set forth below.

PART 389—[AMENDED]

1. The authority citation for Part 389 continues to read as follows:

Authority: Paperwork Reduction Act of 1980, 44 U.S.C. 3501-3520 (1982).

§ 389.101 [Amended]

2. The Table of OMB Control Numbers in § 389.101(b) is amended by inserting "35.26" in numerical order in the section column and "0096" in the corresponding