Subpart C—Management and Supervision of Multiple Family Housing Borrowers and Grant Recipients

2. Section 1930.138 is added to read as follows:

§ 1930.138 Supervisory actions for distressed projects.

Multiple Family Housing projects experiencing high vacancy rates which could lead to project failure can apply for a special servicing market rate rent (SMR) change in accordance with paragraph X of Exhibit C of this subpart.

3. Exhibit C is amended by redesignating current paragraph X as paragraph XI and adding a new paragraph X to read as follows:

Exhibit C of Subpart C—Rent Changes

* * * * *

X. Special Servicing Market Rate Rent (SMR) Change

When a Plan II or Plan II RA RRH project is experiencing severe vacancies due to poor local market conditions, an SMR change may be implemented to attract and keep tenants who could pay more than basic rent. An SMR addresses the situation where some existing and prospective tenants are not willing to pay 30 percent of adjusted income or market rent because the rental rates would exceed those of other rental properties in the community. This action may only be taken after supervisory efforts by FmHA and management efforts by the borrower have not produced an acceptable level of occupancy. For the purposes of this paragraph, market area and community are used as defined in paragraph 2 of Exhibit A–6 of Subpart E of Part 1944.

A. *Eligibility for SMR.* Based on borrower documentation and FmHA servicing records, the District Director will prepare a written recommendation for borrower eligibility for an SMR.

1. Based on borrower documentation and District Office verification:

a. The vacancy rate was at least 15 percent for each month for the most recent 6 month period.

b. Comparable market rents in the community are lower than the previously approved FmHA market rents. Exhibit A–2 to Subpart E of Part 1944 can be used to document comparable market rents.

c. The borrower has aggressively marketed the project including the following actions:

(i) Significant outreach efforts in the community, including (but not limited to) contacts listed in the Affirmative Fair Housing Marketing Plan (AFHMP).

(ii) The borrower had obtained approval from FmHA at least 3 months earlier to rent to ineligible tenants in accordance with paragraph VI B 6 of Exhibit B of this subpart.

d. The borrower complies with FmHA regulations and encourages occupancy through good maintenance and positive relations with tenants.

e. The borrower has provided a signed statement agreeing to forego, without provision to recoup, the return on initial investment while operating with an SMR.

f. The borrower has submitted a project budget on Form FmHA 1930–7, "Statement of Budget and Cash Flow," with only minimally sufficient operation and maintenance expenses. The project budget should continue to fund other cash expenditures such as FmHA payments and the reserve account, except for the return on initial investment which the borrower has agreed to forego according to paragraph X A 1 e of this exhibit.

2. Based on Distric Office servicing actions and documentation:

a. The project has been operational for at least 24 months, except that projects obligated prior to October 1, 1986, must have been operational for at least 6 months. The National Office may make exceptions to these requirements on a case-by-case basis for extreme hardship.

b. No more than 10 percent of budgeted operation and maintenance expenses are reflected in unrestricted cash, or 25 percent if any funds remain from the 2 percent initial operating capital, and reserve account balances do not exceed required levels minus authorized withdrawals.

c. The District Director has reviewed and discussed with the borrower the feasibility of using borrower contributed funds, including advances, in accordance with paragraph XII C of Exhibit B of this subpart.

d. The District Director has reviewed and approved a project budget with only minimally sufficient operation and maintenance expenses and other expenses as specified in paragraph X A 1 f of this exhibit.

e. The District Director has reviewed any market studies or surveys received from MFH loan applicants for the market area and considered any information that may conflict with the request for an SMR.

B. *Approval of SMR.* 1. The State Director may approve the use of an SMR when the conditions listed above in paragraph X A of this exhibit are met.

2. While an SMR is in effect, no initial RRH loan may be obligated for the same market area if existing units can be used to serve the unmet need.

C. *Implementing an SMR.* 1. After the use of an SMR has been approved by the State Director, the District Director will establish an SMR for the project with the borrower.

a. The SMR will be obtained by adjusting Item 3, "FmHA Payment (Principal and Interest) Including Overage," on column 4 of Form FmHA 1930–7, to reflect a payment to FmHA amortized at an interest rate which is less than the full note rate on the borrower's promissory note. The interest rate chosen may never be less than 2 percent.

b. The interest rate of the SMR budget will be set at a level that will make project market rents comparable with community rental rates. This rate will remain constant except as provided in paragraph D of this exhibit.

2. The initial change to SMR rents or a decrease in SMR rents will be accomplished in accordance with paragraph VI B of this exhibit.

D. *Changing an SMR.* 1. An SMR may be increased or decreased whenever the local market conditions warrant, but must be reviewed at least annually.

2. An SMR must be increased by a minimum of 10 percent per year (or a higher amount if mutually agreed to by the borrower and FmHA) when the:

a. Vacancy rate drops to 10 percent or below for 6 consecutive months, or

b. The borrower does not continue to satisfy the conditions of paragraphs X A 1 c (i) and (ii), d, e, or f of this exhibit.

3. An SMR is completely terminated when the market rent is again based on the note interest rate.

4. An increase in an SMR will be accomplished in accordance with paragraph IV of this exhibit.

* * * * *

Dated: August 10, 1987.

Vance L. Clark,

Administrator, Farmers Home Administration.

[FR Doc. 87–22841 Filed 10–1–87; 8:45 am]

BILLING CODE 3410–07–M

DEPARTMENT OF TRANSPORTATION

Federal Aviation Administration

14 CFR Part 39

[Docket No. 87–CE–17–AD; Amdt. 39–5740]

Airworthiness Directives; Cessna Models T303, 310, 320, 335, 340, 401, 402, 404, 411, 414 and 421 Series Airplanes

AGENCY: Federal Aviation Administration (FAA), DOT.

ACTION: Final rule.

SUMMARY: This amendment adopts a new Airworthiness Directive (AD), applicable to Cessna Aircraft Company Models T303, 310, 320, 335, 340, 401, 402, 404, 411, 414 and 421 Series airplanes, equipped with reciprocating engines, herein referred to as 300 and 400 Series airplanes, which requires the modification of the fuel filler ports to prevent inadvertent filling of the fuel tanks with jet fuel. The NTSB has reported six accidents or incidents where airplane misfueling was found to have contributed to these occurrences. The modification is necessary to prevent further misfueling and thereby preclude inflight engine failure.

DATES: *Effective Date:* November 2, 1987.

Compliance: As prescribed in the body of the AD.

ADDRESSES: Cessna Aircraft Company Service Information Letter ME84–31 dated July 20, 1984, applicable to this AD may be obtained from Cessna Aircraft Company, Customer Services, Post Office Box 1521, Wichita, Kansas 67201. This information may be examined in the Rules Docket, Federal

Aviation Administration, Central Region, Office of the Regional Counsel, Room 1558, 601 East 12th Street, Kansas City, Missouri 64106.

FOR FURTHER INFORMATION CONTACT: Mr. Charles Riddle, ACE-140W, Aerospace Engineer, Wichita Aircraft Certification Office, Federal Aviation Administration, 1801 Airport Road, Room 100, Wichita, Kansas 67209; telephone 316-946-4427.

SUPPLEMENTARY INFORMATION: A proposal to amend Part 39 of the Federal Aviation Regulations to include an AD requiring modification of the fuel filler port to prevent inadvertant filling of the fuel tanks with jet fuel on certain Cessna 300 and 400 Series airplanes equipped with reciprocating engines was published in the **Federal Register** on June 8, 1987, (52 FR 21572).

This proposal resulted from a recommendation by the NTSB reporting that there have been six accidents or incidents on Cessna 300 and 400 Series airplanes equipped with reciprocating engines in which misfueling with jet fuel was the cause. Further the board indicated that most cases of misfueling occur with light, twin-engine, piston-powered airplanes which are similar in appearance to turbine engine-powered airplanes.

In recent years, the frequency of accidents involving misfueling with jet fuel has increased significantly despite efforts of the FAA and other interested parties. On September 17, 1982, and October 5, 1984, the FAA issued two Advisory Circulars (ACs) Nos. 20-116 and 20-122, "Marking Aircraft Fuel Filler Openings with Color Decals," and "Anti-Misfueling devices: Their Availability and Uses." Both recommend methods to prevent airplane misfueling. However, the level of response to these AC's has been low considering the nature of the problem and the number of airplanes involved. Therefore, in the interest of aviation safety, the modification of the fuel filler port, recommended by the NTSB, was proposed.

Interested persons have been afforded an opportunity to comment on the proposal. Nine commenters responded. Three of these concurred with the proposal. However, one of these commenters stated that the AD should apply to all turbocharged, single engine piston powered airplanes. The FAA does not agree. Including other manufacturer's airplanes is beyond the scope of this rulemaking action. However, the FAA will consider the commenters suggestion and initiate separate rulemaking actions if appropriate.

The remaining six commenters disagreed with the proposed rule. Three of these commenters felt that the Cessna 336, 337 and P337 Models should not be included in the proposed rule since these airplanes do not resemble any other turbine powered airplanes. In addition, one commenter also objected to the inclusion of the Cessna T303, 310 and 320 Models since these models have had no misfueling accidents. The FAA agrees with the comments on the Cessna 336, 337 and P337 airplanes. Therefore, the proposed rule has been changed by removing these airplanes from the list of those affected. The FAA does not agree with the commenter regarding the T303, 310 and 320 airplanes. There has been one instance of a T310Q airplane being misfueled with Jet-A fuel. The FAA has determined that these models could be mistaken for a turbine powered airplane and therefore, the proposed rule has not been changed in this regard.

Another commenter felt that his 310 did not look like a turbo-prop and should not be affected. He also suggested that the filler ports of turbine powered airplanes be changed to unique configuration that only a matching nozzle would fit.

As stated above the Model 310 can be mistaken for a turbine powered airplane and be misfueled. Further, changing the filler ports on turbine powered airplanes and changing the turbine fuel nozzles would still require a change to the fuel filler ports of piston powered airplanes to prevent the redesigned turbine fuel nozzle from fitting into the fuel port of a piston powered airplane. The FAA has determined that proposed rule is the most economical way to prevent airplane misfueling. Two commenters felt that training of the line personnel doing the refueling is the only acceptable method to prevent misfueling. The FAA agrees that education and training would certainly help in preventing misfueling. However, promulgating requirements with respect to those areas is beyond the scope of this rulemaking. The FAA, has determined that the proposed rule is the best means for preventing misfueling at this time.

One commenter questioned the estimated cost to modify the affected airplanes as compared to the benefit obtained from that modification. The estimated cost was based upon the information currently available in the manufacturers service bulletin. The benefits obtained from this modification is a reduction in the number of accidents involving misfueling with jet fuel. The frequency of this type of accident has increased significantly in recent years. Therefore, in the interest of aviation safety the FAA proposed modification of the fuel filler ports.

Accordingly, the proposal is adopted with the changes noted above. The FAA has determined there are approximately 12,112 airplanes affected by the AD. The estimated cost of modifying these airplanes would depend on the number of fuel filler caps on the airplane. Many of the above airplanes have optional wing or wing locker tanks. The estimated cost to modify the Cessna fleet is $4,933,286. This cost assumes that the optional fuel tanks are installed on those airplanes on which they were offered. The average cost per airplane is $350.

The cost of complying with AD therefore will not have a significant financial impact on any small entities owning affected airplanes.

Therefore, I certify that this action (1) is not a "major rule" under the provisions of Executive Order 12291, (2) is not a "significant rule" under DOT Regulatory Policies and Procedures (44 FR 11034; February 26, 1979) and (3) will not have a significant economic impact on a substantial number of small entities under the criteria of the Regulatory Flexibility Act. A copy of the draft regulatory evaluation has been prepared for this action and has been placed in the public docket. A copy of it may be obtained by contacting the Rules Docket at the location provided under the caption **"ADDRESSES".**

List of Subjects in 14 CFR Part 39

Air transportation, Aviation safety, Aircraft, Safety.

Adoption of the Amendment

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

PART 39—[AMENDED]

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.

§ 39.13 [Amended]

2. By adding the following new AD:

Cessna: Applies to the following airplanes equipped with reciprocating engines certificated in any category:

Model and Serial Number

T303
T30300001 thru T30300301
310 thru 310R

310–39032 thru 310R2140
320 thru 320F
320–0001 thru 320F0045
335
335–0001 thru 335–0065
340 thru 340A
340–0001 thru 340A1543
401 thru 401B
401–0001 thru 401B0221
402 thru 402C
402–0001 thru 402C0653
404
404–0001 thru 404–0859
411 thru 411A
411–0001 thru 411A0300
414 thru 414A
414–0001 thru 414A0858
421 thru 421C
421–0001 thru 421C1257

Compliance: Required as indicated in the body of the AD, unless already accomplished.

To preclude misfueling of the airplane resulting in engine failure, accomplish the following:

(a) Within the next 12 calendar months after the effective date of this AD, unless already accomplished, modify all fuel filler opening(s) in accordance with the instructions contained in Cessna Service Information Letter ME84–31 dated July 20, 1984.

(b) Airplanes may be flown in accordance with FAR 21.197 to a location where this AD may be accomplished.

(c) In accordance with FAR Part 43, Appendix A, Item (c) 29, the modifications required by this AD [except installation of the SK303–29 kit] are preventative maintenance and may be performed by the holder of a pilot certificate issued under FAR Part 61 on airplanes owned or operated by him subject to the limitations of FAR 43.3(g). The maintenance record entries required by FAR 43.9 and FAR 91.173 must be accomplished.

(d) An equivalent means of compliance with this AD may be used if approved by the Manager, Wichita Aircraft Certification Office, Federal Aviation Administration, 1801 Airport Road, Room 100, Wichita, Kansas 67209.

All persons affected by this directive may obtain copies of the document(s) referred to herein upon request to Cessna Aircraft Company, Customer Services, Post Office Box 1521, Wichita, Kansas 67201; or the FAA, Rules Docket, Office of the Regional Counsel, Room 1558, 601 East 12th Street, Kansas City, Missouri 64106.

This amendment becomes effective on November 2, 1987.

Issued in Kansas City, Missouri, on September 17, 1987.

Jerold M. Chavkin,

Acting Director, Central Region.

[FR Doc. 87–22719 Filed 10–1–87; 8:45 am]

BILLING CODE 4910–13–M

SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 275 and 279

[Rel. No. IA–1083; File No. S7–24–86]

Financial and Disciplinary Information That Investment Advisers Must Disclose to Clients

AGENCY: Securities and Exchange Commission.

ACTION: Adoption of rule.

SUMMARY: The Commission is adopting a rule under the Investment Advisers Act of 1940 to codify an investment adviser's fiduciary obligation to disclose material financial and disciplinary information to clients. The rule sets forth the general disclosure obligation and provides guidance on disciplinary information required to be disclosed. The rule is intended to help ensure that clients receive information material to their decision whether to hire or continue to engage an adviser.

EFFECTIVE DATE: December 1, 1987.

FOR FURTHER INFORMATION CONTACT: Debra Kertzman, Attorney, or Robert E. Plaze, Special Counsel, Office of Disclosure and Adviser Regulation, (202) 272–2107, Division of Investment Management, Securities and Exchange Commission, 450 Fifth Street NW., Washington, DC 20549.

SUPPLEMENTARY INFORMATION: The Securities and Exchange Commission ("Commission") today is adopting Rule 206(4)–4 under the Investment Advisers Act of 1940 [15 U.S.C. 80b–1 *et seq.*] ("Advisers Act"). The rule, which was proposed for public comment on September 19, 1986,[1] codifies the Commission's interpretation that section 206 of the Advisers Act [15 U.S.C. 80b–6] requires (1) advisers with custody or discretionary authority over client funds or securities or who require substantial prepayment of advisory fees to disclose precarious financial conditions to clients, and (2) all advisers to disclose material disciplinary events to clients. In addition, the rule specifies certain legal or disciplinary events (referred to hereafter as "disciplinary events") involving the adviser or key advisory personnel as presumptively material. While providing guidance on the types of material disciplinary information required to be disclosed, the rule makes clear that additional disclosure may be required under the Advisers Act.

[1] Investment Advisers Act Rel. No. 1035 (September 19, 1986) [51 FR 34229 (September 26, 1986)].

Discussion

Section 206 of the Advisers Act prohibits investment advisers from engaging in fraudulent and deceptive acts and practices and provides the Commission with rulemaking authority to define and prescribe means reasonably designed to prevent such acts and practices.[2] Fraudulent and deceptive acts and practices under section 206 include the failure to disclose certain facts.[3] The Commission proposed Rule 206(4)–4 to remind advisers of their obligation to disclose to clients material facts about precarious financial conditions and certain disciplinary events, and to provide guidance on some of the disciplinary events required to be disclosed.

Thirty-one comments were received on the proposed rule.[4] Most commenters supported the general purpose of the rule. Many, however, suggested modifications to either clarify the disclosure obligation under the rule or narrow its scope. After reviewing the comments, the Commission has decided to adopt the rule with several modifications. Rule 206(4)–4, as adopted: (1) Limits the requirement to disclose precarious financial conditions to advisers with custody or discretionary authority over client funds or securities, or that require substantial prepayment of advisory fees, (2) requires all advisers to disclose material disciplinary events to clients, and (3) sets forth those disciplinary events that are presumptively material.

1. Financial Information

As proposed, paragraph (a)(1) of the rule would require all advisers to disclose to clients material facts with respect to a financial condition of the adviser that is reasonably likely to impair the adviser's ability to meet contractual commitments to clients ("precarious financial conditions").

[2] Section 206 of the Advisers Act, in relevant part, states that: It shall be unlawful for any investment adviser, by use of the mails or any means or instrumentality of interstate commerce, directly or indirectly: (1) to employ any device, scheme, or artifice to defraud any client or prospective client; (2) to engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client; * * * (4) to engage in any act, practice, or course of business which is fraudulent, deceptive, or manipulative. The Commission shall, for purposes of this paragraph (4) by rules and regulations define, and prescribe means reasonably designed to prevent such acts, practices, and courses of business as are fraudulent, deceptive, or manipulative.

[3] *SEC v. Capital Gains Research Bureau*, 375 U.S. 180, 198 (1963).

[4] File No. S7–24–86 contains these public comment letters as well as a summary of comments prepared by the Commission staff.

Fourteen commenters recommended limiting financial disclosures under the rule to advisers that either have custody of client assets or require substantial prepayment of advisory fees.[5] These commenters stated that an adviser's financial condition is material to a client or prospective client only when client assets or prepaid services may be jeopardized.[6]

The Commission agrees that the financial condition of all advisers may not be material to their clients and has modified the rule accordingly. As adopted, the rule requires only those advisers with custody or discretionary authority [7] over client funds or securities, or that require prepayment of advisory fees of more than $500 per client and six months or more in advance, to disclose a precarious financial condition to clients.[8] Several commenters urged the Commission not to impose this financial disclosure obligation on advisers solely because they have discretionary authority over client assets. They asserted that a client's decision whether to hire an adviser and give it discretionary authority is due primarily to the services the adviser is able to provide, rather than the adviser's financial background. The Commission believes, however, that this information is material to these clients and should be disclosed because of the risk of investment loss resulting from the disruption or discontinuance of active investment management.[9]

[5] These are the circumstances under which an adviser must include a balance sheet in Part II of its Form ADV [17 CFR 279.1]. Form ADV is the registration form for investment advisers. Part II of which specifies disclosures to clients and prospective clients required by Rule 204–3 under the Advisers Act [17 CFR 275.204–3] ("brochure rule").

[6] In addition, several of these commenters requested the Commission to clarify what constitutes a "financial condition reasonably likely to impair the adviser's ability to meet contractual commitments to clients" under the rule. Such a determination is inherently factual in nature but, as noted by two commenters, would generally include insolvency or bankruptcy.

[7] "Discretionary authority" under the rule includes both express and implied discretionary authority. *See Follansbee v. Davis, Skaggs & Co., Inc.*, 681 F.2d 673 (9th Cir. 1982); *Carras v. Burns*, 516 F.2d 215 (4th Cir. 1975).

[8] Under the rule, advisers required to disclose a precarious financial condition need only make such disclosures to those clients over whose securities they have custody or discretionary authority, or from whom they accept substantial prepayment of advisory fees, and not to other clients.

[9] The risk of investment loss is especially acute where the client's portfolio requires constant supervision because it contains volatile, high risk investments, or where clients, such as an investment company or a pension plan, must overcome legal hurdles (shareholder votes, etc.,) to replace the adviser.

2. Material Disciplinary Information

Paragraph (a)(2) of the proposed rule would require an adviser to disclose material facts about any disciplinary event material to an evaluation of the adviser's integrity or ability to meet contractual commitments to clients. Paragraph (b) of the proposed rule defined certain disciplinary events involving the adviser or its management persons and occurring within the past ten years as material.

A number of commenters urged the Commission to revise this paragraph to narrow the definition of material disciplinary events. They stated that this provision of the rule would require advisers to disclose information that they believed to be immaterial. For example, several commenters argued that the rule would require disclosure of a violation of a technical state insurance regulation by an insurance holding company parent of an adviser, although such a violation might not be material to a client's evaluation of the advisory subsidiary's integrity or ability to meet contractual commitments to clients.

Because of these commenters' concerns, the Commission has decided to substantially modify paragraph (b). As adopted, paragraph (b) creates a rebuttable presumption of materiality rather than a determination of materiality. The Commission acknowledges that there are circumstances where some of the disciplinary events set forth in paragraph (b) may not be material to clients. This may be due to differences in the size and organizational structure of an adviser, the broad range of investment-related laws, and/or the length of time which has passed since the disciplinary event occurred.

One option some commenters suggested, and the Commission considered, would be to simply codify the general duty to disclose material disciplinary events and allow case law to determine which events are material and thus required to be disclosed. However, the Commission believes that it is desirable to provide advisers with guidance in complying with their disciplinary disclosure obligation under Section 206. By creating a presumption of materiality, Rule 206(4)–4 will provide this guidance while preserving flexibility for advisers able to rebut the presumption based upon a particular fact situation. To determine whether a disciplinary event falling within the terms of paragraph (b) overcomes the presumption of materiality, an adviser should carefully weigh each of the following four factors: the distance of the entity or individual involved in the disciplinary event from the advisory function, the nature of the infraction that led to the disciplinary event, the severity of the disciplinary sanction, and the time elapsed since the date of the disciplinary event. While there may be particular instances where a single factor is dispositive, all four factors should be considered because in most instances no single factor will be controlling.

a. Pending Criminal Proceedings

Paragraph (b), as proposed, would define certain civil and criminal court actions, agency proceedings, and self-regulatory organization ("SRO") proceedings as material disciplinary events.[10] Included within the definition of material court actions were pending criminal proceedings relating generally to fraud or theft. Several commenters urged the Commission not to define pending criminal proceedings as material disciplinary events under the rule because this would, in their opinion, have the effect of imposing a penalty on the adviser before a finding of guilt is made or, if the case is ultimately dismissed or a finding of innocence is made, unfairly penalize the adviser. The rule has not been modified in this respect. The Commission believes that a pending criminal proceeding against an adviser or its management person is material and should be disclosed because it reflects upon the degree of trust and confidence clients would place in their adviser. Moreover, the requirement to disclose pending criminal proceedings is no different than the disclosure required of directors and executive officers of companies issuing securities,[11] registrants in their annual

[10] The Commission has modified the definition of "investment-related" in paragraph (d)(3) of the rule to conform to the 1986 amendments to section 203(e)(2)(B) of the Advisers Act [15 U.S.C. 80b-3(e)(2)]. Pub. L. 99–571, section 101, 100 Stat. 3208, 3220 (1986). The amendments expanded the circumstances under which an adviser could be disqualified from registration to include felony or misdemeanor convictions involving government securities brokers or dealers or entities or persons required to register under the Commodity Exchange Act [17 U.S.C. 1 *et seq.*].]

[11] *See* Item 11 of Form S–1 [17 CFR 239.11]; Item 18 of Form S–4 [17 CFR 239.25]; Item 21 of Form S–11 [17 CFR 259.18]; Item 10 of Form S–18 [17 CFR 239.28]; Item 9 of Form N–1A [17 CFR 274.11A]; Item 10 of Form N–2 [17 CFR 274.11a-1]; Item 13 of Form N–3 [17 CFR 274.11b]; Item 13 of Form N–4 [17 CFR 274.11c]; Item 6 of Form N–5 [17 CFR 274.5]; and Item 17 of Form N–8B–4 [17 CFR 274.14].

or semi-annual reports,[12] persons soliciting proxies,[13] or persons making a tender offer.[14]

b. Management Persons

Paragraph (b), as adopted, requires disclosure of disciplinary events involving the adviser or its management persons. As defined in paragraph (d), management persons include any person with the power to exercise, directly or indirectly, a controlling influence over the management or policies of an adviser or to determine the general investment advice given to clients. Seven commenters urged the Commission to narrow this definition, asserting it would include too many persons or entities not directly involved in giving investment advice, particularly in the context of a large diversified financial firm. The adoption of the presumptive materiality standard in paragraph (b) effectively limits the breadth of the definition of management person. As discussed above, the distance of the entity or person involved in the disciplinary event from the advisory function is one factor in determining whether the presumption of materiality of a disciplinary event listed under paragraph (b) may be overcome.

One commenter asked the Commission to clarify whether an adviser would have to disclose the disciplinary history of a person no longer employed or affiliated with the investment advisory firm. Under the definition of "management person," an adviser is only required to disclose the disciplinary history of persons currently employed or affiliated with it, regardless of whether the disciplinary event occurred prior to the person's employment or affiliation with the adviser.

c. Time Period

Paragraph (b) of the proposed rule would define certain disciplinary events as material unless more than ten years had elapsed from the time of the event. This ten-year period is based upon the time period specified in section 203(e)(2) of the Advisers Act [15 U.S.C. 80b-3(e)(2)][15] and Item 11 of Form ADV.[16] In the proposing release, the Commission requested comment on whether a different time period should be used, such as the five-year period specified in Item 401(f) of Regulation S-K [17 CFR 229.401(f)].[17]

Several commenters urged the Commission to reduce the time period from ten to five years. According to these commenters, reducing the time period would not eliminate the adviser's obligation to disclose disciplinary events occurring before a five-year period, because paragraph (e) of the rule states that the period specified in paragraph (b) is only a minimum disclosure requirement.

The Commission has decided to adopt the rule with a ten-year period to measure the presumptive materiality of disciplinary events. Because section 203(e)(2) of the Advisers Act reflects a congressional determination that the materiality of disciplinary events involving investment advisers extends back, at a minimum, to events occurring within a ten-year period, a ten-year period is appropriate. The length of this period is mitigated somewhat by the presumptive materiality standard in paragraph (b). As previously discussed, the amount of time that has elapsed is one factor in determining whether the presumption of materiality of a disciplinary event listed under paragraph (b) may be overcome.

Thus, under the rule, disciplinary events involving the adviser or its management person occurring within the ten-year period may, under certain circumstances, not be material to clients and would not have to be disclosed.

3. Integration with Form ADV

Finally, eight commenters recommended that the Commission integrate the disclosure required under Rule 206(4)-4 into Part II of Form ADV (the "brochure"). Use of the brochure to comply with Rule 206(4)-4 would, in their view, make compliance for registered advisers easier and less expensive than a separate disclosure document. The Commission agrees with these commenters and has added a note to Rule 206(4)-4 and an instruction to Form ADV stating that advisers may use their brochure to make the required disclosures,[18] provided that the timing of disclosure provision in paragraph (c) of Rule 206(4)-4 is satisfied.[19]

Regulatory Flexibility Act Analysis

A summary of the Initial Regulatory Flexibility Act Analysis, which the Commission prepared in accordance with 15 U.S.C. 603, regarding proposed Rule 206(4)-4 was published in Investment Advisers Act Release No. 1035. No comments were received on this analysis. The Commission has prepared a Final Regulatory Flexibility Analysis, a copy of which may be obtained by contacting Debra J. Kertzman, Esq., Division of Investment Management, Securities and Exchange Commission, 450 5th Street NW., Washington, DC 20549, (202) 272-2107.

Statutory Authority

The Commission is adopting Rule 206(4)-4 and the instruction of Form ADV under the authority set forth in sections 204, 206(4), and 211(a) of the Advisers Act [15 U.S.C. 80b-4, 80b-6(4) and 80b-11(a)].

List of Subjects in 17 CFR Parts 275 and 279

Investment adviser, Fraud, Securities.

Text of Rule

Parts 275 and 279 of Chapter II of Title 17 of the Code of Federal Regulations is amended as shown:

PART 275—RULES AND REGULATIONS, INVESTMENT ADVISERS ACT OF 1940

1. The authority citation for Part 275 continues to read as follows:

Authority: Sec. 203, 54 Stat. 850, as amended, 15 U.S.C. 80b-3; sec. 204, 54 Stat. 852, as amended, 15 U.S.C. 80b-4; Sec. 206A, 84 Stat. 1433, as added, 15 U.S.C. 80b-6A; sec. 211, 54 Stat. 855, as amended, 15 U.S.C. 80b-11.

2. By adding § 275.206(4)-4 as follows:

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[12] *See* 10 of Form 10-K [17 CFR 249.310]; and sub-item 77e of Form N-SAR [17 CFR 274.101]. *Cf.* Item 11 of Form ADV [17 CFR 279.1].

[13] *See* Item 7 of Schedule 14A [17 CFR 240.14a-10]. *See also* Item 1 of Schedule 14C [17 CFR 240.14C-101] with respect to issuers transmitting information statements.

[14] *See* Item 2 of Schedule 14D-1 [17 CFR 240.14d-100].

[15] Section 203(e)(2) sets forth a list of disciplinary events involving an adviser which can be used to deny, suspend, or revoke an adviser's registration. *See also* Rule 206(4)-3(a)(1) [17 CFR 275.206(4)-3(a)(1)] which prohibits registered investment advisers from using solicitors that have been convicted during the previous ten years of any felony or misdemeanor involving conduct described in section 203(e) of the Advisers Act.

[16] The ten-year period is the minimum disclosure period for disciplinary events in Item 11 of Part I of Form ADV.

[17] Item 401(f) requires issuers to disclose material legal proceedings involving management of the issuer.

[18] One commenter suggested that the Commission allow "insolvent" advisers to give clients a balance sheet to comply with the financial disclosure requirements of Rule 206(4)-4. Under the rule, inclusion of an audited balance sheet in the brochure would not be sufficient to disclose a precarious financial condition: an affirmative statement disclosing such a condition is required.

[19] Under Rule 204-3, registered advisers are required only to offer to deliver a brochure to existing clients. In contrast, under Rule 206(4)-4 disclosure of precarious financial conditions and material disciplinary events must be made promptly to clients.

§ 275.206(4)-4 Financial and disciplinary information that investment advisers must disclose to clients.

(a) It shall constitute a fraudulent, deceptive, or manipulative act, practice, or course of business within the meaning of section 206(4) of the Act for any investment adviser to fail to disclose to any client or prospective client all material facts with respect to:

(1) A financial condition of the adviser that is reasonably likely to impair the ability of the adviser to meet contractual commitments to clients, if the adviser has discretionary authority (express or implied) or custody over such client's funds or securities, or requires prepayment of advisory fees of more than $500 from such client, 6 months or more in advance; or

(2) A legal or disciplinary event that is material to an evaluation of the adviser's integrity or ability to meet contractual commitments to clients.

(b) It shall constitute a rebuttable presumption that the following legal or disciplinary events involving the adviser or a management person of the adviser (any of the foregoing being referred to hereafter as "person") that were not resolved in the person's favor or subsequently reversed, suspended, or vacated are material within the meaning of paragraph (a)(2) of the rule for a period of 10 years from the time of the event:

(1) A criminal or civil action in a court of competent jurisdiction in which the person—

(i) Was convicted, pleaded guilty or nolo contendere ("no contest") to a felony or misdemeanor, or is the named subject of a pending criminal proceeding (any of the foregoing referred to hereafter as "action"), and such action involved: an investment-related business; fraud, false statements, or omissions; wrongful taking of property; or bribery, forgery, counterfeiting, or extortion;

(ii) Was found to have been involved in a violation of an investment-related statute or regulation; or

(iii) Was the subject of any order, judgment, or decree permanently or temporarily enjoining the person from, or otherwise limiting the person from, engaging in any investment-related activity.

(2) Administrative proceedings before the Securities and Exchange Commission, and other federal regulatory agency or any state agency (any of the foregoing being referred to hereafter as "agency") in which the person—

(i) Was found to have caused an investment-related business to lose its authorization to do business; or

(ii) Was found to have been involved in a violation of an investment-related statute or regulation and was the subject of an order by the agency denying, suspending, or revoking the authorization of the person to act in, or barring or suspending the person's association with, an investment-related business; or otherwise significantly limiting the person's investment-related activities.

(3) Self-Regulatory Organization (SRO) proceedings in which the person—

(i) Was found to have caused an investment-related business to lose its authorization to do business; or

(ii) Was found to have been involved in a violation of the SRO's rules and was the subject of an order by the SRO barring or suspending the person from membership or from association with other members, or expelling the person from membership; fining the person more than $2,500; or otherwise significantly limiting the person's investment-related activities.

(c) The information required to be disclosed by paragraph (a) shall be disclosed to clients promptly, and to prospective clients not less than 48 hours prior to entering into any written or oral investment advisory contract, or no later than the time of entering into such contract if the client has the right to terminate the contract without penalty within five business days after entering into the contract.

(d) For purposes of this rule:

(1) "Management person" means a person with power to exercise, directly or indirectly, a controlling influence over the management or policies of an adviser which is a company or to determine the general investment advice given to clients.

(2) "Found" means determined or ascertained by adjudication or consent in a final SRO proceeding, administrative proceeding, or court action.

(3) "Investment-related" means pertaining to securities commodities, banking, insurance, or real estate (including, but not limited to, action as or being associated with a broker, dealer, investment company, investment adviser, government securities broker or dealer, municipal securities dealer, bank, savings and loan association, entity or person required to be registered under the Commodity Exchange Act [7 U.S.C. 1 *et seq.*], or fiduciary).

(4) "Involved" means acting or aiding, abetting, causing, counseling, commanding, inducing, conspiring with or failing reasonably to supervise another in doing an act.

(5) "Self-Regulatory Organization" or "SRO" means any national securities or commodities exchange, registered association, or registered clearing agency.

(e) For purposes of calculating the 10-year period during which events are presumed to be material under paragraph (b), the date of a reportable event shall be the date on which the final order, judgment, or decree was entered, or the date on which any rights of appeal from preliminary orders, judgments, or decrees lapsed.

(f) Compliance with paragraph (b) of this rule shall not relieve any investment adviser from the disclosure obligations of paragraph (a) of the rule; compliance with paragraph (a) of the rule shall not relieve any investment adviser from any other disclosure requirement under the Act, the rules and regulations thereunder, or under any other federal or state law.

Note: Registered investment advisers may disclose this information to clients and pospective clients in their "brochure," the written disclosure statement to clients under Rule 204-3 [17 CFR 275.204-3]; *provided*, that the delivery of the brochure satisfies the timing of disclosure requirements described in paragraph (c) of this rule.

PART 279—FORMS PRESCRIBED UNDER THE INVESTMENT ADVISERS ACT OF 1940

1. The authority citation for Part 279 continues to read as follows:

Authority: The Investment Advisers Act of 1940, 15 U.S.C. 80b-1, *et seq.*

2. By amending instruction 1 to Form ADV, which is described in § 279.1, by adding a new sub-paragraph.

§ 279.1 Form ADV, for Application for Registration of Investment Adviser and for Amendment to Such Registration Statement.

Instruction to Form ADV

1. This is a Uniform Form for use by investment advisers to:

* * * * *

• Comply with their obligation under SEC Rule 206(4)-4 to disclose material financial and disciplinary information to clients. When using Part II of this form to disclose this information to clients, advisers must satisfy the timing of disclosure requirements described in paragraph (c) of SEC Rule 206(4)-4. Note that SEC Rule 206(4)-4(c) requires an adviser to disclose this information promptly to clients, while SEC Rule 204-3(b) only requires an adviser to annually offer to deliver its brochure to existing clients.

* * * * *

By the Commission.
September 25, 1987.
Shirley E. Hollis,
Assistant Secretary.
[FR Doc. 87-22702 Filed 10-1-87; 8:45 am]
BILLING CODE 8010-01-M

DEPARTMENT OF ENERGY

Federal Energy Regulatory Commission

18 CFR Parts 2 and 284

[Docket No. RM87-34-000]

Regulation of Natural Gas Pipelines After Partial Wellhead Decontrol

Issued: September 28, 1987.

AGENCY: Federal Energy Regulatory Commission, DOE.

ACTION: Interim rule; order granting rehearing solely for purposes of further consideration.

SUMMARY: The Federal Energy Regulatory Commission is granting rehearing of Order No. 500 solely for the purpose of affording sufficient time to consider the numerous issues raised in the forty-four requests for rehearing which have been filed. This action does not constitute a grant or denial of rehearing, either in whole or in part.

EFFECTIVE DATE: September 28, 1987.

FOR FURTHER INFORMATION CONTACT: Richard Howe, Jr., Office of General Counsel, Federal Energy Regulatory Commission, 825 North Capitol Street NE., Washington, DC 20426, (202) 357-8274.

SUPPLEMENTARY INFORMATION:

[Docket Nos. RM87-34-001 through RM87-34-045]

Order Granting Rehearing Solely for Purposes of Further Consideration

Before Commissioners: Martha O. Hesse, Chairman; Anthony G. Sousa, Charles G. Stalon, Charles A. Trabandt and C. M. Naeve.

On August 7, 1987, the Federal Energy Regulatory Commission issued Order No. 500[1] responding on an interim basis to the decision of the United States Court of Appeals for the District of Columbia Circuit concerning Order No. 436 in *Associated Gas Distributors v. FERC.*[2] On August 28 and September 3, 4, and 8, 1987, the Commission received forty-four timely requests for rehearing of Order No. 500.

In order to afford sufficient time to consider the numerous issues raised in the rehearing requests, it is necessary to grant rehearing of Order No. 500 for the limited purpose of further consideration.

The Commission orders:

Rehearing of Order No. 500 is hereby granted for the limited purpose of further consideration. This action does not constitute a grant or denial of rehearing, either in whole or in part. As provided in § 385.713(d) of the Commission's Rules of Practice and Procedure, no answers to the requests for rehearing will be entertained by the Commission.

By the Commission.
Kenneth F. Plumb,
Secretary.
[FR Doc. 87-22819 Filed 10-1-87; 8:45 am]
BILLING CODE 6717-01-M

[1] 52 FR 30334 (August 14, 1987).
[2] No. 85-1811 (D.C. Cir. June 24, 1987).

DEPARTMENT OF TRANSPORTATION

Federal Highway Administration

23 CFR Parts 230, 633, and 635

Required Contract Provisions

AGENCY: Federal Highway Administration (FHWA), DOT.

ACTION: Final rule.

SUMMARY: The FHWA is amending regulations pertaining to required contract provisions for Federal-aid construction contracts. The purpose of this final rule is to eliminate duplicative provisions of 23 CFR Part 633 that merely restate requirements contained in other existing regulations. This consists of removing the text of Form PR-1273, Required Contract Provisions, from the Appendix to Part 633 and amending Part 635 to include several requirements which were previously addressed only in the Appendix to Part 633. Form PR-1273 is essentially a convenient collection of contract provisions already required by regulations promulgated by the Federal Highway Administration (FHWA) and other Federal agencies. This action is intended to eliminate the need to amend the regulation through repetitive rulemaking procedures each time the form is revised to incorporate a new or amended requirement duly promulgated by the responsible agency.

EFFECTIVE DATE: This final rule is effective October 2, 1987.

FOR FURTHER INFORMATION CONTACT: Mr. William A. Weseman, Chief, Construction and Maintenance Division, (202) 366-0392, or Mr. Paul Brennan, Office of Chief Counsel, (202) 366-1394, Federal Highway Administration, 400 Seventh Street SW., Washington, DC 20590. Office hours are from 7:45 a.m. to 4:15 p.m., E.T., Monday through Friday.

SUPPLEMENTARY INFORMATION: The regulations currently contained in 23 CFR Part 633, Subpart A require certain contract provisions to be incorporated in each highway construction contract that involves the expenditure of Federal funds (other than direct Federal and Appalachian construction contracts). These provisions which are set forth in Appendix A of the regulation, contain the conditions attached to participation of Federal funds and are imposed under authority administered by the FHWA and several other Federal agencies.

Since Appendix A primarly restates requirements contained in regulations promulgated by the Environmental Protection Agency, Department of Labor, Department of Transportation (DOT), or Office of Management and Budget (OMB), the FHWA has determined that it is an unnecessary procedural burden to revise 23 CFR Part 633 by rulemaking whenever the substantive regulations are revised or amended by the responsible agencies. In order to reduce this paperwork burden and to eliminate the redundancy of regulations, Appendix A, Required Contract Provisions, is being removed from Title 23 of the CFR.

To ensure that all conditions of Federal-aid contracts continue to be authorized pursuant to regulation, it is necessary to amend 23 CFR Part 635 to include the following existing requirements which were previously addressed only in 23 CFR Part 633 and Appendix A: provisions for termination of contract, provisions for subcontracting, provisions for final certification of a project concerning wages and labor classifications, and provisions for record of materials, supplies, and labor. Relative to the record of material, supplies, and labor, the FHWA is also increasing the reporting threshold for the submission of Form PR-47, "Statement of Materials and Labor Used by Contractor of Highway Construction Involving Federal Funds" from $500,000 to $1,000,000 for final construction cost for roadway and bridge projects. This change to the reporting threshold will reduce the burden of data collection on contractors and result in only minor changes in the reported construction usage factors.

In the future, the Required Contract Provisions, presently designated as Form PR-1273, will be redesignated as Form FHWA-1273 and distributed periodically through FHWA's division offices located in each State. This process will keep the contract