the Reorganization Plan provides that each Portfolio will bear any expenses it has incurred incidental to the preparation and carrying out of the Reorganization Plan.

14. A registration statement on Form N–14 containing a combined prospectus/proxy statement has been filed with the SEC. Applicants expect to send the prospectus/proxy statement to shareholders of the Acquired Portfolio in October 1997 for their approval at a meeting of shareholders scheduled to be held on or about November 21, 1997.

15. The consummation of the Reorganization is subject to the following conditions set forth in the Reorganization Plan: (a) the shareholders of the Acquired Portfolio will have approved the Reorganization Plan; and (b) the parties will have received exemptive relief from the SEC with respect to the issues that are the subject of the application. Applicants agree not to make any material changes to the Reorganization Plan that affect the application without prior SEC approval.

Applicants' Legal Analysis

1. Section 17(a) of the Act generally prohibits an affiliated person of a registered investment company, or any affiliated person of such a person, acting as principal, from selling any security to, or purchasing any security from the company. Section 2(a)(3) of the Act defines an ''affiliated person'' of another person to include any person that owns 5% or more of the outstanding voting securities of such other person and any person directly or indirectly controlling, controlled by, or under common control with such other person; or, if the other person is an investment company, any investment adviser of the investment company.

2. Rule 17a–8 under the Act exempts from the prohibitions of section 17(a) mergers, consolidations, or purchasers or sales of substantially all of the assets of registered investment companies that are affiliated persons solely by reason of having a common investment adviser, common directors/trustees, and/or common officers, provided that certain conditions are satisfied.

3. Applicants believe that they may not rely upon rule 17a–8 because the Portfolios may be affiliated for reasons other than those set forth in the rule. Smith Barney owns 5% or more of the outstanding voting securities of the Acquired Portfolio. Because of this ownership, the Acquiring Portfolio may be deemed an affiliated person of an affiliated person of the Acquired Portfolio, and vice versa, for reasons not based solely on their common adviser. Consequently, applicants are requesting an order pursuant to section 17(b) of the Act exempting them from section 17(a) to the extent necessary to consummate the Reorganization.

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

5. Applicants submit that the terms of the Reorganization satisfy the standards set forth in section 17(b), in that the terms are fair and reasonable and do not involve overreaching on the part of any person concerned. Applicants note that the Board, including the disinterested trustees, has reviewed the terms of the Reorganization as set forth in the Reorganization Plan, including the consideration to be paid or received, and has found that participation in the Reorganization is the best interests of each Portfolio and that the interests of the existing shareholders of each Portfolio will not be diluted as a result of the Reorganization. Applicants also note that the exchange of the Acquired Portfolio's assets and certain liabilities for the Acquiring Portfolio shares will be based on the Portfolio's relative net asset values.

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

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 97–27761 Filed 10–20–97; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–39236; File No. SR–DCC–97–04]

Self-Regulatory Organizations; Delta Clearing Corp.; Order Granting Approval of a Proposed Rule Change Relating to the Combining of Options and Repo Procedures

October 14, 1997.

On March 17, 1997, Delta Clearing Corp. (''Delta'') filed with the Securities and Exchange Commission (''Commission'') a proposed rule change (File No. SR–DCC–97–04) pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act'').[1] Delta amended the proposed rule change on May 7, 1997, and May 29, 1997. Notice of the proposal was published in the **Federal Register** on September 3, 1997.[2] No comment letters were received. For the reasons discussed below, the Commission is approving the proposed rule change.

I. Description

The proposal combines Delta's procedures for the clearance and settlement of options trades (''Options Procedures'') and Delta's procedures for the clearance and settlement of repurchase and reverse repurchase (''repo'') agreement transactions (''Repo Procedures'') into one set of procedures entitled the Procedures for the Clearing of Securities and Financial Instrument Transactions (''Combined Procedures'').

The Combined Procedures allow Delta to integrate the processing of options and repo transactions. For example, the Combined Procedures consolidate the definitions of many terms (*e.g.*, contract, position, and holder) to make these terms applicable to both option and repos.[3] The Combined Procedures also clarify that calculations of a participant's exposure limit and the maximum potential system exposure (''MPSE'') are determined on an aggregate system-wide basis by providing for a single uniform definition of these terms and by providing in Section 204 of the Combined Procedures that each participant agrees to conduct all transactions cleared through the system within such participant's exposure limit.[4]

Similarly, Section 307 of the Combined Procedures provides that Delta has a security interest in all money and securities of a participant as security for payment of any liability of such participant to Delta arising from participation in the system. Upon the occurrence of a participant default,[5] Delta may liquidate all of a participant's repo and options positions contained in the defaulting participant's account through one liquidating settlement account established for such participant. The Combined Procedures combine the margin provisions for repos and options to clarify that a participant is required to deposit margin based upon its

[1] 15 U.S.C. 78s(b)(1).

[2] Securities Exchange Act Release No. 38971 (August 26, 1997), 62 FR 46530.

[3] The Combined Procedures also provide for more uniform use of the terms ''repo'' and ''repurchase agreement.''

[4] Both the exposure limit and MPSE are designed to limit Delta's uncollateralized exposure to each participant.

[5] The Combined Procedures contain a new term, ''participant default,'' which means a payment default, a delivery default, a premium default, or a margin default.

aggregate net exposure on its options positions and its term repo positions. The Combined Procedures conform the Options Procedures and Repo Procedures by providing that margin deficits shown on the daily margin report must be deposited at or before the later of 11:00 a.m. or the earliest time practicable following the opening of the Federal Reserve System.[6]

In many places, the Options Procedures and Repo Procedures had inconsistent provisions. The Combined Procedures provide uniform rules for both transactions. For example, the proposed rule change extends certain requirements placed on interdealer brokers for options to interdealer brokers for repos,[7] and the trade reporting method for options is made applicable to repos. Section 2202 of the Combined Procedures also incorporates for options transactions the recently approved rule change [8] to the Repo Procedures permitting participants to deposit treasury notes and treasury bonds as margin and incorporating the schedule of applicable haircuts found in Rule 15c3–1(c)(2)(vi)(A)(*1*) under the Act. Section 2204 of the Combined Procedures provides that deposits are not required if the margin deficit shown on the daily margin report is $50,000 or less.[9]

The Combined Procedures adopt the definition of business day previously applicable to options transactions, which excludes Saturday, Sunday, a day on which banking institutions in New York City are authorized by law to close, and any day on which government securities dealers in New York City are not open for business. The Repo Procedures did not exclude days on which government securities dealers are closed.

The Combined Procedures adopt the graduated fine schedule of the Options Procedures which provide for sanctions of $100 for the first filing of a late trade report, $200 for any second violation occurring within three months of the first violation, and $300 for any subsequent violation occurring within three months of a prior violation. Section 3301 of the Repo Procedures provided that the sanction for filing a late trade report was an amount not to exceed $500.

The Combined Procedures use the terms ''Fed Funds'' and ''Federal Reserve System'' instead of the terms ''central bank funds'' and ''central bank wire system'' used in the Repo Procedures.[10] Like the Options Procedures, the Combined Procedures provide that the suspension or termination of Delta's system will not affect the terms of any existing contract absent the consent of the participant which is party to such contract.[11] As currently applicable for repo participants, Section 213 of the Combined Procedures provides that Delta will on an annual basis send a list of current repo and options participants in Delta's system to all participants.

Under the Combined Procedures, a participant may borrow from Delta on an overnight basis up to 35% of the participant's net positive exposure on its options positions and positions in term repos adjusted for performance margin.[12] Previously, participants could only borrow against their exposure on options. Under Section 2212, if the daily margin report shows that the participant has a net positive exposure after adjustment for performance margin, the participant may request on or before 11:00 a.m. of the morning on which the report is sent that Delta lend to it on an overnight basis cash or treasury securities to the extent available to Delta with a value of not more than 35% of the participant's net positive exposure after adjustment for performance margin. In order to make such overnight loans, Delta will generally transmit securities by 3:00 p.m. that day or will transmit funds by 5:00 p.m. that day.

Some provisions are revised from both the Options Procedures and the Repo Procedures. For example, the waiver of suspension provisions of Section 401 are revised to provide that suspension may be deferred not more than two hours in the event of a margin, premium, or payment default and for such period as Delta determines appropriate in the event of a delivery default if Delta determines that the participant required to make delivery has been unable to obtain the security required to be delivered after a good faith effort and that such failure to deliver is not the result of a change in the participant's financial condition.

Section 206 of the Combined Procedures eliminates the requirement that participants deliver audited reports of their internal accounting controls. Participants will continue to be obligated to deliver to Delta annual audited financial statements.

Under the Combined Procedures, Delta, rather than its clearing bank, assumes the authority and obligation to receive, compare, and transmit trade reports and other reports (Articles 23 and 30); to accent trades for clearance (Sections 2303 and 3003); to provide system software (Section 303); to calculate and maintain margin (Article 22); to transmit, receive, and assign exercise notices and to accept exercise notices for clearance (Article 28); and to reconcile differences with participants (Sections 2303 and 3003).

Section 304 of the Combined Procedures provides that inspection by Delta of participants' records will be at such time as may be reasonably requested by Delta and that the scope of such inspections will be limited to matters related to Delta's procedures, the participant's transactions in Delta's system, and other matters related to Delta's business. Previously, Delta's right of inspection of a participant's books and records was not limited to any subject matter.

II. Discussion

Section 17A(b)(3)(F) of the Act[13] requires that the rules of a clearing agency be designed to assure the safeguarding of securities and funds which are in the custody or control of the clearing agency or for which it is responsible. The Commission believes that the rule change is consistent with Delta's obligations under the Act. By combining its Options Procedures and Repo Procedures into a single Combined Procedures manual, this rule change, among other things, clarifies that Delta's risk management procedures apply to options and repos on an aggregate basis. For example, the Combined Procedures

[6] Section 602 of the Options Procedures required the deposit of margin other than intraday additional margin at or before the settlement time on each business day. Section 2602.1 of the Repo Procedures provided for the deposit of margin other than supplemental or intraday additional margin at or before 11:00 a.m.

[7] Such provisions establish qualification requirements for interdealer brokers, including compliance with Rule 17a–23 under the Act, maintenance of books and records, and necessary operational capacity.

[8] Securities Exchange Act Release No. 37639 (September 4, 1996), 61 FR 48186 (File No. SR–DCC–96–09) (order granting approval of proposed rule change relating to acceptable forms of collateral).

[9] Section 602 of the Options Procedures provided that deposits of additional margin with respect to margin deficits shown on the daily margin report are not required if the amount to be deposited by the participant is $5,000 or less. The Repo Procedures in Section 2602.1 provided that deposits are not required if such amount is $50,000 or less.

[10] The Repo Procedures in various places used the terms ''central bank funds'' and ''central bank wire system.'' The use of these terms was intended to cover the situation where Delta had received authorization to clear trades to be effected by participants through central banks other than the Federal Reserve.

[11] The Repo Procedures provided that the suspension or termination of the operation of the system will not affect the terms of any existing repo agreement.

[12] Performance margin represents an estimate of the net shortfall from the liquidation of a participant's positions at the close of the next business day.

[13] 15 U.S.C. 78q–1(b)(3)(F).

provide that calculations of exposure limit and MPSE are to be determined on an aggregate system-wide basis and that liquidation of a participant's positions will be conducted through one account. By ensuring that Delta has access to all of a participant's assets held at Delta, the proposed rule change assists Delta in the safeguarding of securities and funds which are in Delta's control or for which it is responsible.

III. Conclusion

On the basis of the foregoing, the Commission finds that the proposed rule change is consistent with the requirements of the Act and in particular Section 17A of the Act and the rules and regulations thereunder.

It is therefore ordered, pursuant to Section 19(b)(2) of the Act, the proposed rule change (File No. SR–DCC–97–04) be and hereby is approved.

For the Commission by the Division of Market Regulation, pursuant to delegated authority.[14]

Margaret H. McFarland,

Deputy Secretary.

[FR Doc. 97–27756 Filed 10–20–97; 8:45 am]

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–39241; File No. SR–DCC–97–06]

Self-Regulatory Organizations; Delta Clearing Corp.; Order Approving a Proposed Rule Change Relating to the Clearance and Settlement of Mortgage-Backed Securities Repurchase Agreements

October 14, 1997.

On April 7, 1997, the Delta Clearing Corp. (''DCC'') filed with the Securities and Exchange Commission (''Commission'') the proposed rule change (File No. SR–DCC–97–06) pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (''Act'').[1] On May 12, May 29, June 18, and July 9, 1997, DCC amended the proposed rule change. Notice of the proposal was published in the **Federal Register** on July 30, 1997.[2] No comment letters were received. For the reasons discussed below, the Commission is approving the proposed rule change.

I. Description

The proposal amends DCC's Procedures for the Clearing of Securities and Financial Instrument Transactions (''Procedures'') to allow DCC to clear and settle repurchase agreements and reverse repurchase agreements (''repos'') in which the underlying collateral is book-entry, mortgage-based securities issued by the Federal National Mortgage Association (''FNMA'') or the Federal Home Loan Mortgage Corporation (''FHLMC''). Currently, DCC provides clearance and settlement services for repos in which the underlying collateral is a U.S. Treasury security.[3]

A. Definition of Mortgage-Backed Security

Under the rule change, a mortgage-backed security[4] is defined as a book-entry security which is directly issued by FNMA or FHLMC and whose underlying value is represented by a pool of mortgages accumulated by FNMA or FHLMC through its mortgage origination program and which is designed to receive principal payments using a predetermined principal balance schedule. In addition, the following securities are excluded from the definition of mortgage-backed securities: (i) Securities which are issued in registered or bearer form and therefore cannot be transferred through the Board of Governors of the Federal Reserve System's FedWire communication system, (ii) securities which are not issued or guaranteed directly by FNMA or FHLMC, (iii) securities for which the underlying assets are mortgage-backed securities rather than a pool of mortgages, and (iv) notional, interest only, principal only, accrual, and partial accrual securities and floaters and inverse floaters.[5]

A mortgage-backed security may be either a fixed rate mortgage-backed security or an adjustable rate mortgage-backed security. A fixed rate mortgage-backed security is defined as a mortgage-backed security whose coupon rate is a fixed rate of interest. An adjustable rate mortgage-based security (''ARMS'') is defined as a mortgage-backed security whose coupon rate is a variable rate of interest consisting of an index and a spread to such index and whose underlying collateral consists of adjustable rate mortgages with indices and spreads that parallel those of the ARMS.[6]

B. The Clearing Process

Mortgage-backed securities repo transactions involve two settlement dates. The first settlement date (''on-date'') is the date on which one participant (''selling participant'') delivers participant'') in exchange for the delivery of cash (''delivery money'') by the purchasing participants to the selling participant. The second settlement date (''off-date'') is the date on which the purchasing participant returns to the selling participant the mortgage-backed securities delivered on the on-date in exchange for the return by the selling participant of the delivery money together with interest based upon a rate agreed to by the participants (''repo rate''). DCC generally clears both the on-date and off-date portion of a repo transaction. However, there may be certain repo transactions where DCC clears only the off-date portion of the transaction.[7]

1. Execution and Reporting of Trades

Mortgage-backed securities repo transactions to be cleared by DCC may be entered into directly between the two participants to a transaction and reported to DCC by the participants, or they may be entered into between two participants through the facilities of an authorized broker and reported to DCC by the authorized broker. The terms of the mortgage-backed securities repo transactions will be agreed to by the participants prior to the submission of

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[14] 17 CFR 200.30–3(a)(12).

[1] 15 U.S.C. 78s(b)(1).

[2] Securities Exchange Act Release No. 38868 (July 23, 1997), 62 FR 40872.

[3] According to DCC, the market for repo transactions in mortgage-backed securities is estimated to be approximately 25% to 40% of the size of of the market for repo transactions in Treasury securities. DCC also states that this estimate suggests that the outstanding notional size of the market is between $250 billion to $400 billion with daily turnover at 10% of the notional size. For a description of DCC's procedures regarding the clearance and settlement of repos on Treasury securities, refer to Securities Exchange Act Release No. 36367 (October 13, 1997), 60 FR 54095 [File No. SR–DGOC–94–06] (order approving implementation of new procedures allowing for the clearance and settlement of repos on Treasury Securities).

[4] The Procedures refer to mortgage-backed securities as ''mortgage securities.''

[5] For the definitions of these terms, refer to Schedule A of DCC's filing which is attached as Exhibit A.

[6] Sample indices include: (1) The CD rate, which is the weekly average of secondary market interest rates on six month negotiable certificates of deposit as published by the Federal Reserve Board in its Statistical Release H. 15 (519), Selected Interest Rates; (ii) the LIBOR rate, which is a rate which banks charge others banks for U.S. dollar deposits outside the United States for a specified period; (iii) the 11th District cost of funds index, which is the index made available monthly by the Federal Home Loan Bank Board of the cost of funds to members of the Federal Home Loan Bank 11th District; and (iv) the Treasury index, which is the weekly average yield of the benchmark Treasury securities as published by the Federal Reserve Bank. A sample ARMS could bear interest at LIBOR plus 50 basis points with LIBOR adjusting periodically as specified by the terms of the security.

[7] These transactions are referred to the Procedures as novated repos. Securities Exchange Act Release No. 39065 (September 12, 1997), 62 FR 49547 [File No. SR–DCC–97–03] (order approving proposed rule change).