■ 8. Section 299.5 is amended by:
■ a. Revising the term ''INS form No.'' to read ''Form No.'' in the table heading;
■ b. Revising the term ''INS form title'' to read ''Title'' in the table heading; and by
■ c. Adding the entry for Form ''I–901'' to the table, in proper alpha/numeric sequence.

The addition reads as follows:

§ 299.5 Display of control numbers.

* * * * *

Form No.	Title	Currently assigned OMB control No.
* * * * * * *		
I–901	Fee Remittance For Certain F, J, and M Nonimmigrants.	1653–0034
* * * * * * *		

Dated: June 25, 2004.

Tom Ridge,

Secretary of Homeland Security.

[FR Doc. 04–14961 Filed 6–30–04; 8:45 am]

BILLING CODE 4410–10–P

NATIONAL CREDIT UNION ADMINISTRATION

12 CFR Parts 703 and 704

Investment in Exchangeable Collateralized Mortgage Obligations

AGENCY: National Credit Union Administration.

ACTION: Final rule.

SUMMARY: The National Credit Union Administration (NCUA) is issuing final revisions to its regulations regarding investment in collateralized mortgage obligations (CMOs) to authorize all federal credit unions (FCUs) and corporate credit unions to invest in exchangeable CMOs representing interests in one or more SMBS subject to certain safety and soundness limitations. Currently, NCUA regulations prohibit FCUs and certain corporate credit unions from investing in stripped mortgage backed securities (SMBS) and exchangeable CMOs that represent interests in one or more SMBS. NCUA has safety and soundness concerns with direct investment in SMBS, but recognizes that some exchangeable CMOs representing interests in one or more SMBS may be safe investments for credit unions. This rule will also authorize FCUs and corporate credit unions to accept exchangeable CMOs as assets in a repurchase transaction or as collateral on a securities lending transaction regardless of whether the CMO contains SMBS. Finally, this rule contains miscellaneous technical corrections and minor changes to NCUA's Investment and Deposit Activities rule and Corporate Credit Unions rule.

DATES: This rule is effective August 2, 2004.

FOR FURTHER INFORMATION CONTACT: Steve Sherrod, Senior Investment Officer, Office of Strategic Program Support and Planning (OSPSP) at the above address or telephone (703) 518–6620; Kim Iverson, Senior Investment Officer, Office of Strategic Program Support and Planning, at the above address or telephone (703) 518–6620; George Curtis, Corporate Program Specialist, Office of Corporate Credit Unions at the above address or telephone (703) 518–6640; or Paul Peterson, Staff Attorney, Office of General Counsel, at the above address or telephone (703) 518–6555.

SUPPLEMENTARY INFORMATION:

A. Background

The Federal Credit Union Act permits FCUs and corporate credit unions to purchase mortgage related securities (MRS) subject to such regulations as the NCUA Board may prescribe. 12 U.S.C. 1757(15)(B). NCUA regulations generally permit the purchase of CMOs, a multi-class MRS, but not if the CMO is a stripped mortgage backed security (SMBS). 12 CFR 703.14(d) and 703.16(e); 704.5(c)(5) and (h)(4). SMBS include interest-only CMOs (IOs) and principal-only CMOs (POs).

Currently, many CMO issues contain one or more classes of exchangeable CMOs. An exchangeable CMO represents a beneficial ownership interest in a combination of two or more underlying CMOs, and the owner may pay a fee and take delivery of the underlying CMOs. In many cases, these underlying CMOs include IOs and POs.

Because NCUA regulations prohibit investment in SMBS, the regulations also prohibit investment in an exchangeable CMO that represents an interest in one or more IOs or POs. Certain exchangeable CMOs representing IOs or POs, however, do not carry the risk or raise the same safety and soundness concerns associated with direct investment in an SMBS.

On January 22, 2004, the NCUA Board issued a notice of proposed rulemaking to amend NCUA rules to authorize FCUs and corporate credit unions to invest in an exchangeable CMO representing interests in one or more IOs or POs if the exchangeable CMO meets certain conditions. 69 FR 4886 (February 2, 2004).

The first condition concerned the rate of amortization of the underlying IOs and POs. For an exchangeable CMO representing one or more IOs, the Board proposed that the notional principal of each IO must decline at the same rate as the principal on one or more non-IO CMOs included in the combination. For an exchangeable CMO representing one or more POs, the Board proposed that the principal of each PO must decline at the same rate as the notional principal of one or more IOs included in the combination or at the same rate as the principal on one or more interest-bearing CMOs included in the combination. The Board also proposed a second condition: that, at the time of purchase, the ratio of the market price of the CMO to its remaining principal balance is between .8 and 1.2, meaning that the discount or premium of the market price to par must be less than 20 points. The proposed rule also stated that credit unions may not exercise the right to exchange an exchangeable CMO if it represents an interest in one or more SMBS that would be impermissible for that credit union to hold as a separate investment.

The Board's proposal also contained several definitional changes and other technical corrections to Parts 703 and 704 of NCUA's rules and regulations. In Part 703, the Board proposed to add a definition of ''collateralized mortgage obligation;'' amend the definitions of ''put,'' ''call,'' ''custodial agreement,'' ''derivative,'' and ''european financial options;'' and change the phrase ''nationally recognized statistical rating

agency'' to ''nationally recognized statistical rating organization.'' In Part 704, the Board proposed to add a definition of ''derivative,'' amend the definitions of ''small business related security'' and ''weighted average life,'' and change the phrase ''interest rate risk simulation tests'' to ''interest rate sensitivity analysis requirements.''

B. Summary of Changes From the Proposed Rule

In this final rule, the Board generally adopts the rule as proposed with some variations. The Board will permit the purchase of exchangeable CMOs representing interests in SMBS only if the CMOs satisfy the conditions established in the proposed rule. The final rule differs from the proposed rule as follows: First, the Board believes that CMOs are not appropriate for all credit unions, and notes that those with investment authority at a credit union must be qualified by education or experience to assess the risk characteristics of every investment that they make, including CMOs. Since exchangeable CMOs are a more complex investment, the final rule specifically requires that a credit union seeking to invest in exchangeable CMOs must have the expertise to apply the unique price range and amortization conditions in this rule. Second, the final rule relaxes the proposed conditions on exchangeable CMOs containing SMBS, but only for CMOs that are accepted by the credit union as assets associated with repurchase transactions or as collateral associated with securities lending transactions. Third, the rule clarifies that derivatives in the form of interest rate lock commitments and forward sales commitments on loans originated by the credit union are not prohibited. Fourth, the rule changes the NCUA office to which applications for an Investment Pilot Program should be addressed from the Office of Examination and Insurance to the Office of Strategic Program Support and Planning.

C. Public Comments

NCUA received 30 comment letters regarding the proposed rule. Many commenters supported the exchangeable CMO portion of the proposed rule without reservation, and all but a few of the remaining commenters expressed general support for the Board's intent to allow credit unions to invest in certain exchangeable CMOs containing strips. In addition, the commenters uniformly supported the miscellaneous technical corrections and clarifying amendments.

Comments Requesting Elimination of the Proposed Safety and Soundness Conditions

Several commenters supported authorizing credit unions to purchase exchangeable CMOs representing SMBS without conditions, or with significantly lesser conditions, than those NCUA proposed.

One commenter suggested that NCUA authorize credit unions to buy any exchangeable CMO containing strips, without restriction, so long as the credit union does not exercise the exchange option. This commenter believes a simple statement that the exchange option cannot be exercised is sufficient, and no other conditions are necessary.

Several commenters thought that, for corporate credit unions, NCUA should focus on the interest rate risk associated with the corporate's aggregate portfolio and should not place conditions on particular individual investments such as exchangeable CMOs and strips. These commenters believe that the proposed conditions on the purchase of individual exchangeable CMOs are unnecessary and overly complex in light of the requirement that corporate credit unions conduct a periodic interest rate sensitivity analysis on their investment portfolios and limit their risk exposure as described in § 704.8. 12 CFR 704.8.

Two commenters said NCUA should allow FCUs to invest directly in SMBS, and in exchangeable CMOs containing SMBS, without restriction when used for the purpose of reducing balance sheet risk and earnings volatility.

One commenter suggested that credit unions qualifying under NCUA's Regulatory Flexibility Program, 12 CFR part 742, should be exempt from the Part 703 prohibition on investment in SMBS and any prohibition on exchangeable CMOs representing SMBS.

A few commenters question the need for the proposed rule. One of these commenters stated, ''It appears that the proposed rule is basically seeking to prevent practices that simply do not exist today. Current rules clearly state that investing in IO and PO Strips is not allowed because of the highly volatile nature of theses investments. Exchangeable CMOs are clearly not MBS strips.'' The commenter requests a simple clarification that ''a credit union may not exercise the right to exchange an exchangeable CMO nor undertake any re-engineering of mortgage cash flows that results in the creation of securities that are impermissible under NCUA rules and regulations.''

While the Board appreciates these comments, it is concerned about the volatile and risky nature of SMBS. The Board believes SMBS are generally inappropriate investments for credit unions and are not normally well suited to risk reduction practices such as hedging, even in a well-run credit union or a credit union conducting aggregate portfolio interest rate risk analysis. On the other hand, the Board agrees that very few, if any, of the existing exchangeable CMOs that represent SMBS are overly risky. In fact, the Board believes that all or almost all currently existing exchangeable CMOs satisfy the safety and soundness conditions imposed in the final rule. Nevertheless, the securities market is constantly evolving, and the Board anticipates that, in the future, the market may include exchangeable CMOs representing SMBS that do have the substantive risks of those SMBS. The Board wants to make clear in this rulemaking how federal credit unions and corporate credit unions can determine the permissibility of any exchangeable CMO representing SMBS.

Comments Expressing Concern About the Complexity of Exchangeable CMO Investments

Two commenters remarked on the complexity of the exchangeable CMO investment and thought credit unions that invest in them should demonstrate a complete understanding of how these products work and the risks they entail. Another commenter noted that SMBS are volatile and should only play a limited role, if any, as a core investment. Still another commenter thought NCUA should not authorize credit unions to purchase exchangeable CMOs representing SMBS because of a perceived lack of expertise and sophistication at some credit unions.

The Board appreciates that CMOs may offer a unique risk-reward tradeoff among the various investments permitted for FCUs by the FCU Act, and that CMOs may play an important role in a well-diversified investment portfolio. Still, the Board agrees with these commenters that CMOs are not appropriate investments for all credit unions and notes that NCUA's investment regulation specifically provides that ''those with investment authority [at the FCU] must be qualified by education or experience to assess the risk characteristics of investments and investment transactions.'' 12 CFR 703.3(g). The Board expects FCUs and corporate credit unions to understand each and every investment that they make, including CMOs, and how those investments work. Since exchangeable CMOs are a more complex investment and subject to unique price range and amortization conditions, the final rule

specifically requires that a credit union seeking to invest in exchangeable CMOs must have the expertise to apply the price range and amortization conditions.

Comments on the Proposed Price Range Condition for Exchangeable CMOs Representing SMBS

Most commenters thought the .8 to 1.2 range on the ratio of purchase price to par was a reasonable method to separate out those exchangeable CMOs with risk characteristics substantially similar to the underlying SMBS. Some commenters suggested variations on this condition.

A few commenters suggest NCUA should treat exchangeable CMOs containing PO strips differently from those containing IO strips. These commenters believe NCUA should allow the purchase at less than 80% of par of exchangeable CMOs containing PO strips. One commenter states ''A PO that trades at a steep discount (less than 80% of par) is often less risky than one that trades at par, since it can result in significant gains if paid off early, and it does not have more downside risk than a PO CMO purchased at greater than 80% of par.''

One commenter suggests that, to keep an exchangeable CMO from having the substantive risk characteristics of an IO, NCUA should limit the coupon rate of the exchangeable CMO so that it is no higher than the coupon on the underlying collateral. The same commenter suggests that, to keep the exchangeable CMO from having the substantive risk characteristics of a PO, NCUA should require eligible securities to have a coupon at the time of issuance that is above a readily available index. For example, if the security has an expected weighted average life of 3 years at the time of issuance, the coupon for such security can not be below the yield on a 3 year Treasury plus a set spread, such as 50 basis points.

One commenter suggests that a credit union with adequate staff and resources to monitor an exchangeable CMO would be in the best position to determine acceptable risk tolerances and set premium or discount limits.

As stated above, the Board believes some safety and soundness conditions on exchangeable CMOs representing SMBS are necessary. The conditions in the final rule are simple enough for a credit union to apply but specific enough to ensure that any exchangeable CMO that meets these conditions will not be too risky. Any FCU that wishes to invest in exchangeable CMOs subject to different conditions may always submit an application seeking NCUA approval for an investment pilot program. 12 CFR 703.19.

Comments on the Proposed Amortization Condition for Exchangeable CMOs Representing SMBS

Another commenter asks that NCUA provide more flexibility to allow for underlying IOs to amortize slower than other non-IO portions of exchangeable CMO. The commenter believes this would allow the investing credit union to receive more income over the life of the investment.

The Board notes that if the underlying IO amortized more slowly than the other non-IO portions of the exchangeable CMO, the credit union would eventually hold an exchangeable CMO that represented only an IO and had risk characteristics identical to the underlying IO. This is unacceptable to the Board and demonstrates the need for the amortization condition.

One commenter agreed with the proposed price range restrictions but stated that the amortization limitations do not materially advance NCUA's safety and soundness objectives and may unnecessarily restrict the investment flexibility of FCUs.

Another commenter also supported the ''pre-purchase'' condition, meaning the limit on premium or discount of purchase price to par, but objects to the ''post-purchase'' condition, meaning the amortization requirement. This commenter believes the latter issue is addressed for corporate credit unions by the interest rate modeling of § 704.8, and that ''to require separate risk management requirements specific to exchangeable CMOs is both unnecessary and overly burdensome.''

The Board does not intend that the amortization condition be a ''post-purchase'' condition; that is, that the credit union monitor amortization speeds after purchase. The Board is changing the language of the final rule to clarify that the determination of whether a particular CMO complies with the amortization condition will be made at the time of purchase from estimates of amortization speeds contained in the offering circular or other official information.

Comments on the Proposed Requirement That Credit Unions Not Exercise the Exchange Option if One or More of the Underlying CMOs Is an Impermissible IO or PO

One commenter suggests NCUA allow credit unions that hold otherwise permissible exchangeable CMOs representing IOs or POs to exchange the CMO for the underlying securities if the credit union immediately sells the impermissible IOs or POs resulting from the exchange. This commenter believes this approach will allow the credit union flexibility to make best use of the exchangeable CMO feature.

As stated above, the Board is generally opposed to credit unions holding SMBS. A credit union that invests in exchangeable CMOs representing impermissible SMBS and that would like to exercise the exchange option may, however, submit an investment pilot program for NCUA review and possible approval. 12 CFR 703.19.

Miscellaneous Comments on the Proposed Exchangeable CMO Rule

Several commenters state a final prospectus may not be available for CMOs purchased at time of issue. These commenters ask that, for investments in exchangeable CMOs made before issuance of the final prospectus, NCUA authorize the credit union to rely on a preliminary prospectus to determine if the CMO is exchangeable and, if so, permissible. If the preliminary prospectus does not indicate the CMO will be exchangeable or does not include decrement tables allowing the CU to determine if the underlying investments amortize at the same rate, these commenters want NCUA to allow the credit union to purchase and hold the investment even if the final prospectus indicates the investment is an exchangeable CMO that fails the amortization requirement.

The Board appreciates that credit unions may have difficulty ascertaining if a CMO purchased at or before issuance satisfies the requirements of this final rule. Before committing to purchase, a credit union should use its best efforts to examine the available documentary information to determine if the CMO will satisfy the requirements. If necessary, a credit union may seek assurances of compliance from the issuer. If an FCU uses its best efforts, and then determines after purchase that the CMO fails the requirements of this rule, it should process the investment as specified in its investment policies for investments that fail a requirement of part 703. 12 CFR 703.3(j). Corporate credit unions should process the failed investment under the Investment Action Plan provisions of the corporate rule. 12 CFR 704.10.

Several commenters ask that NCUA provide guidance to credit unions currently holding exchangeable CMOs that fail the requirements in the proposed rule, preferring that NCUA allow credit unions to continue holding

these CMOs. One of these commenters also noted that in 1993 NCUA indicated some CMOs created from SMBS might be permissible. *See* 58 FR 34868 (June 30, 1993) (''The NCUA Board notes that recently some CMOs and REMICs have been created from stripped mortgage-backed securities. These instruments are permitted if they can pass the high-risk security tests.'') This 1993 statement has lead the commenter to believe that there is no regulatory prohibition on CMOs containing strips.

As stated above, the Board believes that few, if any, existing exchangeable CMOs will fail the conditions established in this final rule. Any CMOs that do fail the conditions should be processed under the FCU's investment policies or, for corporate credit unions, under an Investment Action Plan. 12 CFR 703.3(j), 704.10. While the NCUA recognized in 1993 that some CMOs had been created from SMBS and that they might be permissible if they passed the high-risk securities test (HRST), any CMO that had substantially the same risk characteristics as the underlying SMBS would likely have failed the HRST. NCUA regulations no longer require HRS testing. To ensure that credit unions do not hold exchangeable CMOs with significant risks from the underlying SMBS, those CMOs must satisfy the conditions provided in this final rule.

One corporate credit union commenter is particularly concerned about the effect of the rule on repurchase transactions. FCUs and corporate credit unions may only accept as repurchase assets those assets in which they can invest directly, and this commenter believes it will be difficult to identify and cull out impermissible exchangeable CMOs. 12 CFR 703.13(c)(1), 704.5(d)(2). The commenter states that, since credit unions are a small portion of the repurchase market, it is improbable that repurchase custodians will restrict repurchase assets to those CMOs qualifying under this proposal. Given the speed and volume of repurchase transactions, the commenter believes it would be onerous for a credit union to review each CMO that is part of the repurchase transaction to ensure it complies with this proposal.

The Board appreciates the commenter's concerns about the difficulties in separating out impermissible assets and collateral in these transactions. The Board also notes that, in both repurchase transactions and securities lending transactions, a credit union relies primarily on the creditworthiness of the counterparty to get its money back and only secondarily on the repurchase asset or securities lending collateral. The potential for interest rate risk and price volatility associated with CMOs representing interests in SMBS is less significant in these transactions. Accordingly, the Board is amending parts 703 and 704 to indicate that exchangeable CMOs representing interests in SMBS may be used as assets or collateral in investment repurchase transactions or securities lending transactions, and the price range and amortization conditions need not be applied to exchangeable CMOs used in this way.

One commenter seeks clarification that the rule applies to both privately issued and federally issued CMOs. The Board intends that the rule apply to all exchangeable CMOs, regardless of issuer.

Miscellaneous Comments on the Exchangeable CMO Rule

Two commenters suggested that NCUA modify the proposed exchangeable CMO definition, and references to CMOs in the rule text, to reflect that the purchase of a CMO is an investment in a particular class of a CMO structure, not in an instrument that is a multi-class CMO structure. The Board agrees with the commenter and amends the final rule text as suggested.

One commenter states credit unions should set aggregate investment limits, not NCUA. Another commenter states NCUA should amend the call report to obtain additional detail on exchangeable CMOs. These issues are beyond the scope of the proposed rule and are not addressed in the final rule.

Comments on the Proposed Miscellaneous Technical Corrections and Clarifying Amendments

One commenter states that, if NCUA does not intend with its proposed change to the definition of derivative to expand or contract permissible types of investments for credit unions, it should say so.

The Board does not intend, through its changes to the derivative definition and other provisions of parts 703 and 704 that reference that definition, to either expand or contract the universe of investments currently permissible for FCUs and corporate credit unions.

D. Other Changes in the Final Rule

The Board is making additional changes not triggered by specific public comment. The Board proposed to change the definition of derivative so it would track the definition of derivative instrument used under generally accepted accounting principles (GAAP) while excluding those derivatives that, under GAAP, do not have to be recognized as an asset or liability in the statement of financial condition and be valued at fair market value. The Board's intent was to ensure that: (1) The regulatory definition of derivative is consistent with the accounting definition; and (2) embedded options in an otherwise permissible investment that are not significant enough to require separate accounting under GAAP would not cause that investment to be considered a prohibited derivative. The final rule retains the Board's intent but achieves it through different rule text. Instead of excluding embedded options from the regulatory definition of derivative, the final rule recognizes them as derivatives but excludes them from the general prohibition on derivatives.

Recently, the GAAP definition of derivative evolved to include loan commitments that relate to the origination of mortgage loans that will be held for sale. Financial Accounting Standards Board Statement of Financial Accounting Standards No. 149, *Amendment of Statement 133 on Derivative Instruments and Hedging Activities,* paragraph 6(c). FCUs routinely enter into loan commitments such as interest rate lock commitments and forward sales commitments on mortgage loans they originate for sale, and the Board supports such commitments when used in a prudent manner. Since NCUA will now tie the regulatory definition of derivative to the GAAP definition, the general prohibition on derivatives could be interpreted to prohibit these types of commitments. Accordingly, the final rule clarifies that derivatives in the form of interest rate lock commitments and forward sales commitments on loans FCUs originate are excluded from the general prohibition on derivatives. Similarly, for corporate credit unions, the general prohibition on derivatives excludes forward sales commitments on loans originated by another credit union where the corporate intends to purchase the loan.

Currently, the responsibility for receipt and initial processing of applications under the Investment Pilot Program rests with NCUA's Office of Examination and Insurance. 12 CFR 703.19(c). The final rule transfers that responsibility to NCUA's Office of Strategic Program Support and Planning.

Regulatory Procedures

Regulatory Flexibility Act

The Regulatory Flexibility Act requires NCUA to prepare an analysis to

describe any significant economic impact a proposed rule may have on a substantial number of small credit unions (those under $10 million in assets). This rule expands the investment authority granted to FCUs and corporate credit unions. The rule will not have a significant economic impact on a substantial number of small credit unions and, therefore, a regulatory flexibility analysis is not required.

Paperwork Reduction Act

NCUA has determined that the final rule would not increase paperwork requirements under the Paperwork Reduction Act of 1995 and regulations of the Office of Management and Budget. NCUA currently has OMB clearance of part 703 and part 704 collection requirements. *See* OMB No. 3133–0133 for 12 CFR part 703, and OMB No. 3133–0129 for 12 CFR part 704.

Executive Order 13132

Executive Order 13132 encourages independent regulatory agencies to consider the impact of their actions on state and local interests. In adherence to fundamental federalism principles, NCUA, an independent regulatory agency as defined in 44 U.S.C. 3502(5), voluntarily complies with the executive order. The executive order states that: ''[n]ational action limiting the policymaking discretion of the states shall be taken only where there is constitutional and statutory authority for the action and the national activity is appropriate in light of the presence of a problem of national significance.'' Portions of the rule apply to all corporates that accept funds from federally insured credit unions, including state chartered corporates. The Board believes that the protection of such credit unions from unwarranted investment in risky investments, and ultimately the National Credit Union Share Insurance Fund (NCUSIF), warrants application of the proposed rule to all corporates, including both state chartered and nonfederally insured. The rule does not impose additional costs or burdens on the states or affect the states' ability to discharge traditional state government functions. NCUA has determined that this rule may have an occasional direct effect on the states, on the relationship between the national government and the states, or on the distribution of power and responsibilities among the various levels of government. However, the potential risk to the NCUSIF without the final changes justifies them.

The Treasury and General Government Appropriations Act, 1999—Assessment of Federal Regulations and Policies on Families

The NCUA has determined that this rule would not affect family well-being within the meaning of section 654 of the Treasury and General Government Appropriations Act, 1999, Pub. L. 105–277, 112 Stat. 2681 (1998).

Small Business Regulatory Enforcement Fairness Act

The Small Business Regulatory Enforcement Act of 1996 (Pub. L. 104–121) provides generally for congressional review of agency rules. A reporting requirement is triggered in instances where NCUA issues a final rule as defined by section 551 of the Administrative Procedure Act. 5 U.S.C. 551. The Office of Management and Budget is reviewing whether this rule is a major rule for purposes of the Small Business Regulatory Enforcement Fairness Act of 1996.

List of Subjects

12 CFR Part 703

Credit unions, Investments.

12 CFR Part 704

Corporate Credit unions, Reporting and Recordkeeping Requirements.

By the National Credit Union Administration Board on June 24, 2004.

Becky Baker,

Secretary of the Board.

■ For the reasons stated in the preamble, NCUA amends 12 CFR part 703 and 12 CFR part 704 as follows:

PART 703—INVESTMENT AND DEPOSIT ACTIVITIES

■ 1. The authority citation for part 703 continues to read as follows:

Authority: 12 U.S.C. 1757(7), 1757(8), 1757(15).

■ 2. Amend § 703.2 to revise the definitions of *Call, Custodial Agreement, Derivatives*, and *Put*, and add definitions of *Collateralized Mortgage Obligation* and *Exchangeable Collateralized Mortgage Obligation*, as follows:

§ 703.2 Definitions.

* * * * *

Call means an option that gives the holder the right to buy a specified quantity of a security at a specified price during a fixed time period.

* * * * *

Collateralized Mortgage Obligation (CMO) means a multi-class mortgage related security.

* * * * *

Custodial Agreement means a contract in which one party agrees to hold securities in safekeeping for others.

* * * * *

Derivatives means any derivative instrument as defined under generally accepted accounting principles (GAAP).

* * * * *

Exchangeable Collateralized Mortgage Obligation means a class of a collateralized mortgage obligation (CMO) that, at the time of purchase, represents beneficial ownership interests in a combination of two or more underlying classes of the same CMO structure. The holder of an exchangeable CMO may pay a fee and take delivery of the underlying classes of the CMO.

* * * * *

Put means an option that gives the holder the right to sell a specified quantity of a security at a specified price during a fixed time period.

* * * * *

■ 3. Amend § 703.8 by revising the second sentence of paragraph (b)(3) to read as follows:

§ 703.8 Broker-dealers.

* * * * *

(b) * * *

(3) * * * The Federal credit union should consider current financial data, annual reports, reports of nationally-recognized statistical rating organizations, relevant disclosure documents, and other sources of financial information.

* * * * *

■ 4. Amend § 703.9 by revising the second sentence of paragraph (d) to read as follows:

§ 703.9 Safekeeping of investments.

* * * * *

(d) * * * The Federal credit union should consider current financial data, annual reports, reports of nationally-recognized statistical rating organizations, relevant disclosure documents, and other sources of financial information.

* * * * *

■ 5. Amend § 703.14 to revise paragraph (g)(4) and paragraph (g)(13) introductory text to read as follows:

§ 703.14 Permissible investments.

* * * * *

(g) * * *

(4) The options' expiration dates are no later than the maturity date of the share certificate.

* * * * *

(13) The Federal credit union provides its board of directors with a monthly report detailing at a minimum:

* * * * *

■ 6. Amend § 703.16 to revise paragraphs (a) and (e) and add paragraph (f) to read as follows:

§ 703.16 Prohibited investments.

(a) *Derivatives.* A Federal credit union may not purchase or sell financial derivatives, such as futures, options, interest rate swaps, or forward rate swaps. This prohibition does not apply to:

(1) Any derivatives permitted under §§ 701.21(i) and 703.14(g) of this chapter;

(2) Embedded options not required under GAAP to be accounted for separately from the host contract; and

(3) Interest rate lock commitments or forward sales commitments made in connection with a loan originated by the Federal credit union.

* * * * *

(e) *Stripped mortgage backed securities (SMBS).* A Federal credit union may not invest in SMBS or securities that represent interests in SMBS except as described in paragraphs (1) and (3) below.

(1) A Federal credit union may invest in and hold exchangeable collateralized mortgage obligations (exchangeable CMOs) representing beneficial ownership interests in one or more interest-only classes of a CMO (IO CMOs) or principal-only classes of a CMO (PO CMOs), but only if:

(i) At the time of purchase, the ratio of the market price to the remaining principal balance is between .8 and 1.2, meaning that the discount or premium of the market price to par must be less than 20 points;

(ii) The offering circular or other official information available at the time of purchase indicates that the notional principal on each underlying IO CMO should decline at the same rate as the principal on one or more of the underlying non-IO CMOs, and that the principal on each underlying PO CMO should decline at the same rate as the principal, or notional principal, on one or more of the underlying non-PO CMOs; and

(iii) The credit union staff has the expertise dealing with exchangeable CMOs to apply the conditions in paragraphs (e)(1)(i) and (e)(1)(ii) of this section.

(2) A Federal credit union that invests in an exchangeable CMO may exercise the exchange option only if all of the underlying CMOs are permissible investments for that credit union.

(3) A Federal credit union may accept an exchangeable CMO representing beneficial ownership interests in one or more IO CMOs or PO CMOs as an asset associated with an investment repurchase transaction or as collateral in a securities lending transaction. When the exchangeable CMO is associated with one of these two transactions, it need not conform to the conditions in paragraphs (e)(1)(i) and (ii) of this section.

(f) *Other prohibited investments.* A Federal credit union may not purchase residual interests in collateralized mortgage obligations, real estate mortgage investment conduits, or small business related securities.

■ 7. Amend § 703.19 by revising the introductory language of paragraph (c) to read as follows:

§ 703.19 Investment Pilot Program.

* * * * *

(c) A third-party seeking approval of an investment pilot program must submit a request to the Director of the Office of Strategic Program Support and Planning that addresses the following items:

* * * * *

PART 704—CORPORATE CREDIT UNIONS

■ 8. The authority citation for part 704 continues to read as follows:

Authority: 12 U.S.C. 1762, 1766(a), 1781, and 1789.

■ 9. Amend § 704.2 to add definitions of *Derivatives* and *Exchangeable collateralized mortgage obligation,* and to revise the definitions of *Small business related security* and *Weighted average life,* as follows:

§ 704.2 Definitions.

* * * * *

Derivatives means any derivative instrument as defined under generally accepted accounting principles (GAAP).

* * * * *

Exchangeable collateralized mortgage obligation means a class of a collateralized mortgage obligation (CMO) that, at the time of purchase, represents beneficial ownership interests in a combination of two or more underlying classes of the same CMO structure. The holder of an exchangeable CMO may pay a fee and take delivery of the underlying classes of the CMO.

* * * * *

Small business related security means a security as defined in section 3(a)(53) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(53)), *e.g.*, a security that is rated in 1 of the 4 highest rating categories by at least one nationally recognized statistical rating organization, and represents an interest in 1 or more promissory notes or leases of personal property evidencing the obligation of a small business concern and originated by an insured depository institution, insured credit union, insurance company, or similar institution which is supervised and examined by a Federal or State authority, or a finance company or leasing company. This definition does not include Small Business Administration securities permissible under § 107(7) of the Act.

* * * * *

Weighted average life means the weighted-average time to the return of a dollar of principal, calculated by multiplying each portion of principal received by the time at which it is expected to be received (based on a reasonable and supportable estimate of that time) and then summing and dividing by the total amount of principal.

* * * * *

■ 10. Amend § 704.5 by revising paragraphs (h)(1) and (h)(4) and adding paragraph (h)(5) to read as follows:

§ 704.5 Investments.

* * * * *

(h) * * *

(1) Purchasing or selling derivatives, except for embedded options not required under GAAP to be accounted for separately from the host contract or forward sales commitments on loans to be purchased by the corporate credit union;

* * * * *

(4) Purchasing mortgage servicing rights, small business related securities, residual interests in collateralized mortgage obligations, residual interests in real estate mortgage investment conduits, or residual interests in asset-backed securities; and

(5) Purchasing stripped mortgage backed securities (SMBS), or securities that represent interests in SMBS, except as described in subparagraphs (i) and (iii) below.

(i) A corporate credit union may invest in exchangeable collateralized mortgage obligations (exchangeable CMOs) representing beneficial ownership interests in one or more interest-only classes of a CMO (IO CMOs) or principal-only classes of a CMO (PO CMOs), but only if:

(A) At the time of purchase, the ratio of the market price to the remaining principal balance is between .8 and 1.2, meaning that the discount or premium

of the market price to par must be less than 20 points;

(B) The offering circular or other official information available at the time of purchase indicates that the notional principal on each underlying IO CMO should decline at the same rate as the principal on one or more of the underlying non-IO CMOs, and that the principal on each underlying PO CMO should decline at the same rate as the principal, or notional principal, on one or more of the underlying non-PO CMOs; and

(C) The credit union investment staff has the expertise dealing with exchangeable CMOs to apply the conditions in paragraphs (h)(5)(i)(A) and (B) of this section.

(ii) A corporate credit union that invests in an exchangeable CMO may exercise the exchange option only if all of the underlying CMOs are permissible investments for that credit union.

(iii) A corporate credit union may accept an exchangeable CMO representing beneficial ownership interests in one or more IO CMOs or PO CMOs as an asset associated with an investment repurchase transaction or as collateral in a securities lending transaction. When the exchangeable CMO is associated with one of these two transactions, it need not conform to the conditions in paragraphs (h)(5)(i)(A) or (B) of this section.

■ 11. Amend § 704.8 by revising paragraph (a)(4) to read as follows:

§ 704.8 Asset and liability management.

(a) * * *

(4) Policy limits and specific test parameters for the interest rate sensitivity analysis requirements set forth in paragraph (d) of this section; and

* * * * *

[FR Doc. 04–14762 Filed 6–30–04; 8:45 am]

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DEPARTMENT OF TRANSPORTATION

Federal Aviation Administration

14 CFR Part 39

[Docket No. 2002–NM–223–AD; Amendment 39–13699; AD 2004–13–17]

RIN 2120–AA64

Airworthiness Directives; Fokker Model F.28 Mark 0070 and 0100 Series Airplanes

AGENCY: Federal Aviation Administration, DOT.

ACTION: Final rule.

SUMMARY: This amendment supersedes an existing airworthiness directive (AD), applicable to certain Fokker Model F.28 Mark 0070 series airplanes, that currently requires a one-time inspection to detect loose bolts attaching the gustlock counter-bracket to the pulley on the elevator tension regulator (control) assembly, and corrective action if necessary. This AD instead requires a modification of the elevator tension control mechanism. This AD also revises the applicability to include additional airplanes. The actions specified by this AD are intended to prevent restricted elevator movement and consequent reduced controllability of the airplane. This AD is intended to address the identified unsafe condition.

DATES: Effective August 5, 2004.

The incorporation by reference of certain publications listed in the regulations is approved by the Director of the Federal Register as of August 5, 2004.

ADDRESSES: The service information referenced in this AD may be obtained from Fokker Services B.V., P.O. Box 231, 2150 AE Nieuw-Vennep, the Netherlands. This information may be examined at the Federal Aviation Administration (FAA), Transport Airplane Directorate, Rules Docket, 1601 Lind Avenue, SW., Renton, Washington; or at the National Archives and Records Administration (NARA). For information on the availability of this material at NARA, call (202) 741–6030, or go to: *http://www.archives.gov/federal_register/code_of_federal_regulations/ibr_locations.html.*

FOR FURTHER INFORMATION CONTACT: Tom Rodriguez, Aerospace Engineer, International Branch, ANM–116, FAA, Transport Airplane Directorate, 1601 Lind Avenue, SW., Renton, Washington 98055–4056; telephone (425) 227–1137; fax (425) 227–1149.

SUPPLEMENTARY INFORMATION: A proposal to amend part 39 of the Federal Aviation Regulations (14 CFR part 39) by superseding AD 2000–09–11, amendment 39–11720 (65 FR 30529, May 12, 2000), which is applicable to certain Fokker Model F.28 Mark 0070 series airplanes, was published in the **Federal Register** on April 15, 2004 (69 FR 19950). The proposed AD would require modifying the elevator tension control mechanism and revising the applicability to include additional airplanes.

Comments

We provided the public the opportunity to participate in developing this AD. No comments have been submitted on the proposed AD or on the determination of the cost to the public.

Conclusion

We have carefully reviewed the available data and determined that air safety and the public interest require adopting the AD as proposed.

Cost Impact

This AD affects about 75 airplanes of U.S. registry. The actions take about 1 work hour per airplane, at an average labor rate of $65 per work hour. Required parts will be provided to operators at no cost. Based on these figures, the cost impact of the AD on U.S. operators is estimated to be $4,875, or $65 per airplane.

The cost impact figure discussed above is based on assumptions that no operator has yet accomplished any of the requirements of this AD action, and that no operator would accomplish those actions in the future if this AD were not adopted. The cost impact figures discussed in AD rulemaking actions represent only the time necessary to perform the specific actions actually required by the AD. These figures typically do not include incidental costs, such as the time required to gain access and close up, planning time, or time necessitated by other administrative actions.

Regulatory Impact

The regulations adopted herein will not have a substantial direct effect on the States, on the relationship between the national Government and the States, or on the distribution of power and responsibilities among the various levels of government. Therefore, it is determined that this final rule does not have federalism implications under Executive Order 13132.

For the reasons discussed above, I certify that this action (1) is not a ''significant regulatory action'' under Executive Order 12866; (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, positive or negative, on a substantial number of small entities under the criteria of the Regulatory Flexibility Act. A final evaluation has been prepared for this action and it is contained in the Rules Docket. A copy of it may be obtained from the Rules Docket at the location provided under the caption **ADDRESSES.**

List of Subjects in 14 CFR Part 39

Air transportation, Aircraft, Aviation safety, Incorporation by reference, Safety.