Your letter of May 28, 1992 requests our assurance that we would not recommend that the Commission take any enforcement action against money market funds that purchase certain certificates guaranteed by the Small Business Administration (the "SBA"), as more fully described in your letter.

Your letter states that the certificates are based upon and backed by pools comprised of SBA-guaranteed loans made by private lenders. The SBA guarantees the timely payment of principal and interest on the certificates, whether or not the principal and interest is collected from the issuers of the loans. 1/ The SBA guarantee is backed by the full faith and credit of the United States Government. 2/ The certificates pay interest at a variable rate that resets no less frequently than annually. The securities amortize fully over 20-25 years, but may be called for redemption earlier.

Since the certificates you describe have a final maturity of greater than thirteen months, and since they do not have demand features, they may be purchased by money market funds only if they meet the requirements of paragraph (d)(1) of rule 2a-7 under the Investment Company Act of 1940. 3/ Paragraph (d)(1) provides that "an instrument that is issued or guaranteed by the United States government or any agency thereof which has a variable rate of interest readjusted no less frequently than every 762 days shall be deemed to have a maturity equal to the period remaining until the next readjustment of the interest rate." 4/

The certificates you describe meet the requirement of paragraph (d)(1) that they be "Issued or guaranteed by the United States government or an agency thereof." The Small Business Administration is an agency of the United States, 5/ and its

1/ See 13 CFR §120.711.

2/ See 15 USC §634(g)(3); 13 CFR §120.701.

3/ Except for purchases of Government securities made pursuant to paragraph (c)(2)(ii) of rule 2a-7.

4/ While paragraph (d)(1) requires that the rate of interest paid be readjusted no less frequently than every 762 days, if the interest rate is readjusted less frequently than every 397 days the fund may not use the amortized cost method. See paragraph (c)(2)(ii) of rule 2a-7.

5/ See 15 USC §633(a).
guarantee is in turn guaranteed by the United States government. 6/ Therefore, assuming that upon reset of the interest rate the certificates can reasonably be expected to have a market value that approximates their par value, the requirements of paragraph (d)(1) are satisfied. 7/

Accordingly, on the basis of the facts and representations contained in your letter, we would not recommend enforcement action to the Commission under rule 2a-7 if money market funds purchased the SBA-guaranteed certificates you describe.

Eli Nathans
Special Counsel

---


7/ While the language in paragraph (d)(1) does not explicitly provide that the instruments covered by that paragraph must have a market value that approximates their par value upon the readjustment of the interest rate, this requirement is implicit in the rule. In adopting rule 2a-7, the Commission stated that the rule "is designed to limit the permissible portfolio instruments of a money market fund . . . to those instruments that have a low level of volatility and thus will provide greater assurance that the money market fund will continue to be able to maintain a stable price per share that fairly reflects the current net asset value per share of the fund." Investment Company Act Rel. No. 13380 (July 8, 1983). This interpretation of paragraph (d)(1) would preclude a fund from relying on that paragraph when purchasing instruments with floating rates that may not rise above a preset cap. We understand, based on a telephone conversation between Eli Nathans of the staff and John Good, counsel to Morgan Keegan, held on June 3, 1992, that none of the instruments that Morgan Keegan seeks to sell to money market funds will have caps on the movement of interest rates.
May 28, 1992

VIA FEDERAL EXPRESS

Office of Chief Counsel
Division of Investment Management
Securities and Exchange Commission
450 Fifth Street N.W.
Washington, D.C. 20549
Attn: Thomas S. Harman, Esq.

Re: Morgan Keegan & Company, Inc.

Ladies and Gentlemen:

We are outside general counsel to Morgan Keegan & Company, Inc. (the "Broker"), and we submit this letter on the Broker's behalf. The Broker desires to sell in initial offering and secondary market transactions to investment companies characterized as "money market funds" (the "Purchasers") certain certificates hereinafter described (the "Securities") that are guaranteed by the United States Small Business Administration (the "SBA"). Based on the following facts and legal analysis, and assuming that, in each case of purchase of Securities by a Purchaser, the Purchaser will be in compliance with investment criteria described in said Purchaser's prospectus, we respectfully request that the Division of Investment Management (the "Division") issue a no-action letter stating that no enforcement action will be recommended against either the Broker or the Purchasers under the Investment Company Act of 1940 (the "1940 Act") if the Broker sells the Securities to the Purchasers in initial offering and secondary market transactions.

Legal Opinion

Based on the facts and authorities hereinafter stated, it is our opinion that the Securities (i) are Government securities, as defined in §2(a)(16) of the 1940 Act, (ii) are supported by the full faith and credit of the United States, (iii) have a remaining maturity of less than 397 calendar days for purposes of Rule 2a-7 under the 1940 Act (the "Rule"), and (iv) otherwise conform with the Rule in all material respects.
Facts

Description of the Broker

The Broker is a full service, regional broker/dealer firm registered under and operating pursuant to §15 of the Securities Exchange Act of 1934 (the "1934 Act"), and is a member of the New York Stock Exchange and the National Association of Securities Dealers. The Broker has historically been a significant dealer and broker of debt securities issued by the United States government and agencies/instrumentalities thereof or corporations backed thereby, including Federal National Mortgage Association ("FNMA"), Federal Home Loan Mortgage Corporation ("Freddie Mac") and Student Loan Marketing Association ("Sallie Mae"). The Broker is an approved Pool Assembler under SBA regulations and routinely assembles pools of SBA guaranteed loans, causes the SBA's Fiscal and Transfer Agent to issue certificates with respect to said pools (the "Securities") and sells the Securities to the Broker's customers in public offerings and secondary dealer market transactions.

Description of the Securities

The Securities consist of certificates issued by the SBA's fiscal and transfer agent based upon pools of SBA guaranteed loans (or portions thereof) assembled by the Broker as an approved pool assembler. The Securities are commonly referred to as "floaters" because the interest rate with respect to a particular Security resets up as market rates increase and resets down as market rates decrease. Typically, there are no caps, upward or downward, in the movement of interest rates with respect to the Securities. The interest rate with respect to a Security is readjusted either monthly or quarterly, depending on the particular certificate, with no Securities having a readjustment rate exceeding one (1) year. Adjustments are based on a publicly-available index, typically New York prime, less a fixed margin of interest rate (e.g. prime minus 187 basis points). Due to the frequency of the changes in the interest rates, there is an active and relatively stable secondary trading market in the Securities, in which market the Broker is an active dealer.

The pools consist of SBA guaranteed loans originated primarily by commercial banks. The average size of the SBA loan pool backing a particular SBA certificate is $2 million to $10 million. SBA regulations govern the maximum acceptable difference between lowest and highest interest rates with respect to individual guaranteed loans or portions comprising a particular pool as well as the maximum acceptable difference between maturity dates of such loans or guaranteed portions. The Securities amortize fully over maturities of 20 to 25 years, but may be called for redemption due to prepayment or default with respect to all loans or guaranteed portions comprising the underlying SBA pool. Holders of the Securities receive monthly payments of principal and interest. In most respects, the Securities operate the same as most other mortgage or asset-backed securities in terms of payment of principal and interest, prepayments and secondary market trading.
Legal Analysis

Structure of the SBA

The Small Business Administration is an agency of the United States government under the general direction and supervision of the President of the United States. 15 USCS §633(a). The administrator of the SBA is appointed from civilian life by the President, by and with the advice and consent of the United States Senate. 15 USCS §633(b). Funding of the SBA programs is obtained through the annual budgetary process, and the SBA is authorized to issue notes to the United States Treasury, which is directed to purchase said notes, to meet its obligations pursuant to its loan and guaranty programs. 15 USCS §633(c). SBA policy with respect to its lending and guaranty functions is set by a Loan Policy Board, the members of which are the SBA Administrator, the Secretary of the Treasury and the Secretary of Commerce. 15 USCS §633(d). The SBA is empowered to make or guarantee loans to qualified small business concerns in amounts consistent with its annual funding limits pursuant to the various appropriation acts passed by Congress from time to time and consistent with policies set forth by the Loan Policy Board. 15 USCS §636. In furtherance of the SBA's power to make and guarantee loans, the Administrator has the power to prescribe regulations pursuant to which he may cause the SBA to assign or sell publicly or privately any evidence of debt, contract, claim, personal property or security assigned to and/or held by the SBA in connection with the payment of loans granted under the Act and to make such other rules and regulations he deems necessary to effect the purpose of the Act. 15 USCS §634(b).

Authority to Issue or Guarantee Securities

The SBA is directed to guarantee timely payment of principal and interest with respect to certificates that are based on and backed by a pool or pools comprised solely of SBA-guaranteed loans made by private lenders. 13 C.F.R. §120.701. The SBA's guaranty of such certificates is backed by the full faith and credit of the United States. Id. The SBA's Fiscal and Transfer Agent (the "FTA") under the supervision of the SBA and pursuant to rules adopted by the SBA and published in the Federal Register, issues the SBA guaranteed certificates in denominations prescribed by the SBA, which certificates are transferable on the books and records of the SBA or the FTA. 13 C.F.R. §120.707. The FTA is responsible for the administration of each pool, and each certificate will be self-liquidating as the result of borrower prepayments, SBA redemption and borrower payments, and/or payment by the SBA by reason of its guaranty of the principal and interest. 13 C.F.R. §120.709. Finally, and perhaps most importantly, the SBA guarantees the timely payment on the payment date, whether or not collected, of interest and principal installments, and any prepayments or other early recoveries of principal on loans, as undertaken in the SBA's guaranty appearing on the face of the certificates. 13 C.F.R. §120.711.

Status of SBA Certificates as Government Securities

Section 2(a)(16) of the 1940 Act defines a Government security as "any security issued or guaranteed as to principal or interest by the United States, or by a person controlled or supervised by and acting as an instrumentality of the Government of the United States pursuant to authority granted by the Congress of the United States; or any certificate of deposit for any of the foregoing." Section 2(a)(36) of the 1940 Act defines the term "security" as any "note, stock, treasury stock, bond, debenture, evidence of indebtedness ... or any certificate of interest
The SBA certificates described in this letter are clearly Government securities within the meaning as set forth above and in Rule 2a-7 under the 1940 Act. The certificates are issued by a Fiscal and Transfer Agent acting on behalf of the SBA, which, as described above, is an agency of the United States created by and acting pursuant to a grant of authority by the Congress of the United States. Moreover, the timely payment of interest and principal with respect to the certificates is guaranteed by the SBA, and the SBA's guaranty is backed by the full faith and credit of the United States.

The SBA certificates are quite similar to certificates and/or notes issued by Sallie Mae and Fannie Mae, which the Division has previously addressed in no action letters.

In 1989, the Division stated that it would not pursue enforcement action in respect to the sale of Sallie Mae notes to money market funds on the basis that such notes were government securities as defined in §2(a)(16) of and Rule 2a-7 under the 1940 Act. See Student Loan Marketing Association (SEC No-Action Letter, Available 1/18/89). In its request for a no-action letter, Sallie Mae emphasized its establishment by act of Congress, its board of directors being comprised of 7 members appointed by the President and its status as an "agency" for purposes of the Federal Reserve System open market operations.

Moreover, in 1988 the Division addressed the status of Fannie Mae as an instrumentality of the United States government and concluded that the organization was excluded from the coverage of the 1940 Act as an instrumentality of the United States, despite its private ownership. See Federal National Mortgage Association (SEC No-Action Letter, Available 1/25/88).

Both Sallie Mae and Fannie Mae may be owned by private individuals or corporations and have civilian board members who are not appointed by members of the United States government. The SBA, on the other hand, is specifically designated as an agency of the United States, its administrator is appointed by the President with the advice and consent of the Senate and its Loan Policy Board consists of cabinet members. Inasmuch as by statute its guarantees and loans are backed by the full faith and credit of the United States and by regulation its loan pool certificates are likewise supported, it is our opinion that the SBA certificates are government securities within the meaning of §2(a)(16) of the 1940 Act.

Suitability for Purchase by Money Market Funds

Moreover, it is our opinion that the Securities are acceptable portfolio securities for registered money market funds pursuant to Rule 2a-7 under the 1940 Act. The Rule sets forth standards as to diversification, credit risk and average maturity for portfolios of money market funds which criteria are designed to allow such funds to (i) maintain a stable net asset value (typically $1.00 per share), (ii) minimize credit risk, and (iii) minimize interest rate risk. Under the Rule, a money market fund may acquire Government securities in unlimited amounts, without regard to diversification rules. See I.C. Release No. 18005, (CCH Fed. Sec. Law Rep. ¶84,710 at 81,321). Moreover, Government securities purchased by a money market fund may have maturity dates up to 762 calendar days after the date of purchase, provided that if the fund uses an amortized cost method of valuation, such maturity dates may be no more
than 397 days. 12 C.F.R. §270.2a-7(c)(2). Generally, the Purchaser must maintain a dollar-weighted average maturity for its entire portfolio of ninety days or less. 12 C.F.R. §270.2a-7(e)(2)(iii). The maturity date of a Government security bearing a variable interest rate is the period from the time of purchase until the time of the next readjustment of the interest rate. 12 C.F.R. §270.2a-7(d)(1); see also I.C. Release No. 18005, (CCH Fed. Sec. Law Rep. ¶84,710 at 81,326).

It is also our opinion that the Securities contain all of the foregoing features designed to ensure price stability and risk protection for money market funds. The Securities have interest readjustment dates not exceeding 397 days, with most of the Securities having interest readjustment dates of 90 days or less and none of the Securities having interest readjustment dates in excess of one (1) year. Therefore, the Securities do not violate Reg. §270.2a-7(c)(c)(2)(i). Due to the relatively short readjustment periods, much of the interest rate risk (and, consequently, price volatility) associated with the Securities is minimized, and the purchase of the Securities is unlikely to cause the purchasing fund to violate the rule requiring a 90 day or less dollar-weighted average portfolio maturity. It is unlikely that investment in the Securities would cause a money market fund to "break a dollar". The Securities are supported by the full faith and credit of the United States, therefore rendering them eligible securities for money market fund purchase.

The Division, in Student Loan Marketing Association (SEC No-Action Letter, Available 1/18/92), determined not to take enforcement action in respect to the purchase by money market funds of long term Sallie Mae floating rate notes having maturities from one to ten years but with interest rates being reset every 7 days. Such notes were represented by Sallie Mae in its request letter as characteristics much the same as characteristics of the underlying student loans, in much the same way as the SBA certificates described above bear the characteristics of the underlying SBA guaranteed loans. I submit that the characteristics of the Securities are similar enough to the characteristics of the Sallie Mae notes addressed in the foregoing no-action letter to warrant a like response in the instant case.

Based on our opinions expressed above that the Securities (i) are Government securities, backed by the full faith and credit of the United States, (ii) have a maturity date of less than 397 days, and (ii) conform in all material respects with the rules set forth in Rule 2a-7, and assuming that, in each case of purchase of Securities by a Purchaser, the Purchaser will be in compliance with investment criteria described in said Purchaser’s prospectus, we hereby respectfully request that the Division issue a no-action letter stating that it will not take enforcement action against either the Broker or money market funds purchasing Securities in the event the Broker should sell Securities in the manner described above. Please call the undersigned at (901) 685-2550 at your earliest convenience if you should have any questions regarding the Securities or the proposed transactions, or prior to taking formal action if you are inclined to issue a formal letter adverse to that requested above. Your prompt consideration of this request is most appreciated. We have enclosed seven copies of this letter in accordance with current SEC procedures.

Sincerely,
McDonnell Boyd

John A. Good