DEPARTMENT OF THE TREASURY

Fiscal Service

31 CFR Part 344

[Department of the Treasury Circular, Public Debt Series No. 3–72]

United States Treasury Certificates of Indebtedness, Treasury Notes, and Treasury Bonds—State and Local Government Series

AGENCY: Bureau of the Public Debt, Fiscal Service, Department of the Treasury.

ACTION: Final rule.

SUMMARY: The Department of the Treasury hereby publishes a final rule governing United States Treasury Certificates of Indebtedness, Notes, and Bonds of the State and Local Government Series (SLGS). These securities are available for purchase, as provided in this offering, by State and local governments and certain other entities with proceeds (or amounts treated as proceeds) which are subject to yield restrictions or arbitrage rebate requirements under the Internal Revenue Code. The securities are characterized in the regulations as time deposit, demand deposit, and special zero interest.

This final rule sets out the regulatory requirements which stem from the Department of the Treasury's new processing environment for United States Treasury Certificates of Indebtedness, Notes, and Bonds of the State and Local Government Series.

The Bureau of the Public Debt is implementing operational and regulatory changes expected to benefit investors by providing streamlined procedures, a centralized processing facility, and improved customer services.

DATES: January 23, 1995.

FOR FURTHER INFORMATION CONTACT: Fred Pyatt, Director, Division of Special Investments, Bureau of the Public Debt (304) 480–7752, Ed Gronseth, Deputy Chief Counsel, or Jim Kramer-Wilt, Attorney-Adviser, Office of the Chief Counsel, Bureau of the Public Debt (304) 480–5190.

SUPPLEMENTARY INFORMATION:

I. Background

On October 6, 1994, the Department of the Treasury published a proposed rule in the **Federal Register** (59 FR 50874) to revise regulations codified at 31 CFR part 344. The comment period expired October 21, 1994. No comments were received. These regulations were last revised on July 7, 1989, at 54 FR 28752, with technical corrections published July 7, 1993, at 58 FR 31908.

In 1992, the Bureau of the Public Debt established the Division of Special Investments at its offices in Parkersburg, West Virginia (WV). The primary mission of the Division of Special Investments has been to provide policy guidance and direction for the SLGS securities program. The Division has reviewed the processing environment and is implementing operational and regulatory changes which are expected to benefit investors in United States Treasury securities of the State and Local Government Series by providing streamlined procedures, a centralized processing facility, and improved customer services.

Prior to the effective date of this final rule, the Bureau of the Public Debt authorized selected Federal Reserve Banks or Branches, acting as fiscal agents of the United States, to provide services in connection with the purchase of, transactions involving, and redemption of SLGS securities. Subscriptions for the purchase of SLGS securities were accepted at designated Federal Reserve Banks or Branches, subject to verification by the Bureau of the Public Debt. Full payment for each subscription was required to be available in an account for debit by the Federal Reserve Bank or Branch on or before the date of issue.

This processing environment required that staffing and technical expertise be maintained at 12 designated Federal Reserve Banks or Branches. The Bureau of the Public Debt, Office of Securities and Accounting Services, Division of Special Investments (hereafter referred to as the Division of Special Investments) has determined that the volume of transactions in this securities program does not merit the expense of maintaining technical expertise at 12 different locations.

The Bureau of the Public Debt has decided to centralize issuance, funds collection, and accounting functions for the SLGS securities program in the Division of Special Investments. The responsibility for these functions is withdrawn from the designated Federal Reserve Banks beginning with issues dated January 30, 1995.

After centralization, Federal Reserve Bank or Branch involvement in this program will be limited to processing interest and redemption payments made through reserve account credits for a very small number of existing securities accounts. This method of payment is limited to securities for which subscriptions were submitted prior to February 1, 1987. More than 98% of all interest and redemption payments for SLGS securities are made by the Automated Clearing House method (ACH), with credit directed to the owner's account at a financial institution.

Beginning on the effective date of the final rule, subscriptions for the purchase of SLGS securities which request issuance on or after January 30, 1995, will only be accepted by the Division of Special Investments. Full payment for each subscription will be submitted by the investor's financial institution on or before the issue date utilizing the Fedwire funds transfer system which is available throughout the commercial banking industry.

This final rule provides investors in SLGS securities with several benefits. Investors will enjoy a higher level of customer service and more consistent application of the regulations pertaining to this securities program. Investors will be dealing directly with staff in the Division of Special Investments who are trained in the unique aspects of SLGS securities and whose principal responsibility it is to manage the SLGS securities program.

In addition, United States taxpayers will benefit in terms of the reduced costs of operating this program which will be realized by centralizing operations within the Division of Special Investments.

II. Section by Section Summary

Most of the changes effected by this final rule are ministerial. For example, to provide new addresses and to remove certain references to the Federal Reserve Banks. The final rule also provides for facsimile transmission of most materials under this offering and provides new procedures concerning amending subscriptions (§ 344.3(b)(3)(iv) and § 344.7(b)) and concerning waivers and fees associated with the failure to settle subscriptions (§ 344.4(b) and § 344.8(b)).

Subpart A—General Information

Provisions included in the general information section apply to time deposit, demand deposit, and special zero interest SLGS securities. Noteworthy changes from the 1989 rule are as follows:

(1) Section 344.0—The term ''date telecopied'' for material sent by facsimile equipment is defined as the date transmitted as it appears on the document received. In the case of other carrier services, the term ''date-stamp'' is defined as the date affixed by the carrier service upon the carrier's taking receipt of the material.

(2)–(3) Section 344.1(a) and Section 344.1(b)—The agency's Parkersburg, WV, address is substituted for its former Washington, DC, address.

Subpart B—Time Deposit Securities

Time deposit Treasury securities are offered to State and local government investors to enable these investors to satisfy yield restrictions prescribed by the Internal Revenue Code and regulations. Noteworthy changes from the 1989 rule are as follows:

(1) Section 344.2(b)—Reference to the Federal Reserve Banks as a receiving point for initial subscriptions has been deleted. This final rule expressly allows for sending of initial subscriptions by facsimile equipment (FAX) or other carriers, in addition to postal delivery.

(2) Section 344.2(c)(2)—This section clarifies the authority governing Automated Clearing House payments on account of United States securities.

(3) Section 344.2(c)(2)(iii)—This section clarifies that fiscal agency checks, rather than Treasury checks, are an alternative payment mechanism for securities for which subscriptions were submitted prior to February 1, 1987.

(4) Section 344.3(a)—Reference to the Federal Reserve Banks as the receiving point for subscriptions for purchase of securities under this offering, as well as the reference to in person delivery to such Banks, have been deleted. In addition, this final rule expressly allows for sending of initial subscriptions by facsimile equipment. Whether subscriptions are sent by FAX, mail or other carrier, subscribers are encouraged to expedite delivery.

(5) Section 344.3(b)(1)—This section expressly allows sending of initial subscriptions by facsimile and other carriers. In addition, the Bureau of the Public Debt is substituted for the Federal Reserve Banks to reflect the consolidation of program administration in Parkersburg, WV.

(6) Section 344.3(b)(3)—This section requires that amendments to initial subscriptions be filed on or before the issue date, by 3:00 p.m., Eastern time. In addition, this section permits sending of amendments to initial subscriptions by facsimile, provided the notification is clearly identified as an amendment and is immediately followed by the submission by mail or other carrier of written notification of the amendment.

(7) Section 344.3(b)(3)(i)—This section clarifies that an amendment to an initial subscription may not change the issue date to require issuance earlier than the issue date originally specified. In this section, the Bureau of the Public Debt is substituted for the Federal Reserve Banks to reflect the consolidation of program administration in Parkersburg, WV. This final rule requires that changes under this section be submitted no later than 3:00 p.m., Eastern time, one business day before the originally specified issue date.

(8) Section 344.3(b)(3)(iv)—This new section governs amendments to initial subscriptions which are not submitted timely. Where an amendment is not submitted timely, the Division of Special Investments may determine, pursuant to the provisions governing waiver of regulations set forth under 31 CFR 306.126, that such an amendment is acceptable on an exception basis. Where an amendment is determined to be acceptable on an exception basis, the amended information shall be used as the basis for issuing the securities, and an administrative fee of $100 per subscription will be assessed. The Secretary reserves the right to reject amendments which are not submitted timely.

(9) Section 344.3(c)—In this section, the Bureau of the Public Debt is substituted for the Federal Reserve Banks to reflect the consolidation of program administration in Parkersburg, WV. This final rule requires that a final subscription must be submitted by 3:00 p.m., Eastern time, on or before the issue date.

(10) Section 344.4(a)—This section requires that the issue date selected by the subscriber must be a business day and allows for the sending of initial subscriptions by facsimile or other carrier. In this section, the Bureau of the Public Debt is substituted for the Federal Reserve Banks. Under this final rule, full payment for each subscription must be submitted utilizing the Fedwire funds transfer system.

(11) Section 344.4(b)—The 1989 regulations provided that any subscriber which fails to make settlement on a subscription once submitted is ineligible thereafter to subscribe for securities under this offering for a period of six months. This final rule provides that the Division of Special Investments may determine to waive the six month penalty, pursuant to the provisions governing waiver of regulations set forth under 31 CFR 306.126. Where settlement occurs after the proposed issue date and the Division of Special Investments determines, pursuant to 31 CFR 306.126, that settlement is acceptable on an exception basis, the six month penalty will be waived, and the subscriber shall be subject to a late payment assessment. The assessment will include payment of an amount equal to the amount of interest that would have accrued on the securities from the proposed issue date to the date of settlement, as well as an administrative fee of $100 per subscription. Assessments under this subsection are due on demand. Failure to pay an assessment shall render the subscriber ineligible thereafter to subscribe for securities under this offering until the assessment is paid.

(12) Section 344.5(b)(2)—This section adds a reference to a designated Treasury form and deletes a reference to wire as an authorized means of submitting notice for redemption prior to maturity. The agency's Parkersburg, WV, address is substituted for its former Washington, DC, address. This final rule expressly allows that the notice of redemption may be sent by facsimile or by other carriers, and provides that notice be submitted no less than 15 calendar days and no more than 60 calendar days before the requested redemption date.

(13) Section 344.5(b)(3)(ii)—This section clarifies that the applicable rate table for determining the ''current borrowing rate'' is the one in effect on the day the request for early redemption is telecopied, postmarked, or where delivered by other carrier, date-stamped.

Subpart C—Demand Deposit Securities

The Tax Reform Act of 1986 imposed arbitrage rebate requirements on issuers of tax-exempt bonds and directed the Department of the Treasury to accommodate such requirements by enabling entities to invest qualifying funds in a Treasury money-market type investment vehicle. Accordingly, the Department expanded the SLGS securities program, beginning with its 1986 regulations, to include a demand deposit security offering. This security is not treated as investment property for purposes of sections 143(g)(3) and 148 of the Internal Revenue Code and, therefore, enables eligible entities to invest proceeds of tax-exempt bonds in an obligation which avoids the earning of arbitrage subject to rebate. Noteworthy changes from the 1989 rule are as follows:

(1) Section 344.7(a)—In this section the Bureau of the Public Debt is substituted for the Federal Reserve Banks to reflect the consolidation of program activities in Parkersburg, WV. This final rule clarifies that subscriptions may be submitted by certified or registered mail, or by other carrier. In addition, this final rule provides that a subscription may be submitted by facsimile equipment, at least three business days before the issue date, provided that the original subscription form is submitted by mail, or other carrier, and is received by the Bureau of the Public Debt by 3:00 p.m., Eastern time, on the issue date.

(2) Section 344.7(b)—This section provides that the principal amount to be invested may be changed without penalty on or before the issue date, but no later than 1:00 p.m., Eastern time, on the issue date. This final rule allows for sending of amendments to original subscriptions by facsimile, provided the notification is clearly identified as an amendment and is immediately followed by the submission, by mail or other carrier, of written notification of the amendment. Where an amendment is not submitted timely, the Division of Special Investments may determine, pursuant to the provisions governing waiver of regulations set forth under 31 CFR 306.126, that such an amendment is acceptable on an exception basis. Where an amendment is determined to be acceptable on an exception basis, the amended information shall be used as the basis for issuing the securities, and an administrative fee of $100 per subscription will be assessed. The Secretary reserves the right to reject amendments which are not submitted timely.

(3) Section 344.8(a)—In this section, the Bureau of the Public Debt is substituted for the Federal Reserve Banks to reflect the consolidation of program activities in Parkersburg, WV. This final rule requires that full payment for each subscription be submitted utilizing the Fedwire funds transfer system.

(4) Section 344.8(b)—The 1989 regulations provided that any subscriber which fails to make settlement on a subscription once submitted is ineligible thereafter to subscribe for securities under this offering for a period of six months. Under this final rule, the Division of Special Investments may determine to waive the six month penalty, pursuant to the provisions governing waiver of regulations set forth under 31 CFR 306.126. Where settlement occurs after the proposed issue date and the Division of Special Investments determines, pursuant to 31 CFR 306.126, that such settlement is acceptable on an exception basis, the six month penalty will be waived, and the subscriber shall be subject to a late payment assessment. The assessment will include payment of an amount equal to the amount of interest that would have accrued on the securities from the proposed issue date to the date of settlement, as well as an administrative fee of $100 per subscription. Assessments under this subsection are due on demand. Failure to pay an assessment shall render the subscriber ineligible thereafter to subscribe for securities under this offering until the assessment is paid.

(5) Section 344.9(b)—The Bureau of the Public Debt is substituted for the Federal Reserve Banks to reflect the consolidation of program activities in Parkersburg, WV. This final rule expressly allows for sending of the notice of redemption by facsimile or by other carriers. The notice must show the account number and the tax identification number of the subscriber. Under this section, the notice must be received at the Bureau of the Public Debt by 1:00 p.m., Eastern time, one business day prior to the requested redemption date.

Subpart D—Special Zero Interest Securities

To give investors flexibility in investing certain proceeds that may become subject to yield restrictions, a new special zero interest security was offered for the first time with the 1989 rule. Under the terms of this offering, subscribers are not required to certify that as of the date of investment all the proceeds subject to yield restrictions are being invested in SLGS securities. With exceptions, this offering is the same as that for time deposit securities. Noteworthy changes from the 1989 rule are as follows:

Section 344.13—This final rule adds a reference to a designated Treasury form and deletes a reference to wire as an authorized means of submitting notice for redemption prior to maturity. The agency's Parkersburg, WV, address is substituted for its former Washington, DC, address. In addition, the section allows for sending of the notice for redemption by facsimile or by other carriers. Under this final rule, notice is to be submitted no less than 15 calendar days and no more than 60 calendar days before the requested redemption date.

Procedural Requirements

It has been determined that this rule is not a significant regulatory action as defined in Executive Order 12866. Therefore, the regulatory review procedures contained therein do not apply.

Although this final rule was issued in proposed form to secure the benefit of public comment, the rule relates to matters of public contract and procedures for U.S. securities, as well as the borrowing power and fiscal authority of the United States. Accordingly, pursuant to 5 U.S.C. 553(a)(2), the notice, public comment, and delayed effective date provisions of the Administrative Procedure Act are inapplicable. As no notice of proposed rulemaking was required, the provisions of the Regulatory Flexibility Act (5 U.S.C. 601, et seq.) do not apply.

The collections of information contained in this final rule have been previously reviewed and approved by the Office of Management and Budget, in accordance with the requirements of the Paperwork Reduction Act (44 U.S.C. 3507) under control number 1535–0091. The rule does not impose a new collection of information requirement.

List of Subjects in 31 CFR Part 344

Bonds, Government securities, Securities.

Dated: January 17, 1995.

Gerald Murphy,

Fiscal Assistant Secretary.

For the reasons set out in the preamble, 31 CFR Chapter II, Subchapter B, Part 344 is revised to read as follows:

PART 344—REGULATIONS GOVERNING UNITED STATES TREASURY CERTIFICATES OF INDEBTEDNESS—STATE AND LOCAL GOVERNMENT SERIES, UNITED STATES TREASURY NOTES—STATE AND LOCAL GOVERNMENT SERIES, AND UNITED STATES TREASURY BONDS—STATE AND LOCAL GOVERNMENT SERIES

Subpart A—General Information

Sec.
344.0 Offering of securities.
344.1 General provisions.

Subpart B—Time Deposit Securities

344.2 Description of securities.
344.3 Subscription for purchase.
344.4 Issue date and payment.
344.5 Redemption.

Subpart C—Demand Deposit Securities

344.6 Description of Securities.
344.7 Subscription for purchase.
344.8 Issue date and payment.
344.9 Redemption.

Subpart D—Special Zero Interest Securities

344.10 General.
344.11 Description of securities.
344.12 Subscription for purchase.
344.13 Redemption.
Appendix A to Part 344—Early Redemption Market Change Formulas and Examples

Authority: 31 U.S.C. 3102, *et seq.*

Subpart A—General Information

§ 344.0 Offering of securities.

(a) In order to provide issuers of tax exempt securities with investments which allow them to comply with yield restriction and arbitrage rebate provisions of the Internal Revenue Code, the Secretary of the Treasury offers for sale the following State and Local Government Series securities:

(1) Time deposit securities:

(i) United States Treasury Certificates of Indebtedness,

(ii) United States Treasury Notes, and

(iii) United States Treasury Bonds.

(2) Demand deposit securities—United States Treasury Certificates of Indebtedness.

(3) Special zero interest securities:

(i) United States Treasury Certificates of Indebtedness.

(ii) United States Treasury Notes.

(b) As appropriate, the definitions of terms used in Part 344 are those found in the relevant portions of the Internal Revenue Code and regulations. The term ''government body'' refers to issuers of State or local government bonds described in section 103 of the Internal Revenue Code, as well as to any other entity subject to the yield restrictions in sections 141–150 of the Internal Revenue Code, or the arbitrage rebate requirements in sections 143(g)(3) or 148 of the Internal Revenue Code. The term ''postmark date'' refers to the date affixed by the U.S. Postal Service, not to a postage meter date. The ''date telecopied'' for material sent by facsimile equipment is the date transmitted, as it appears on the document received. The term ''date-stamp'' refers to the date affixed by the carrier service upon the carrier's taking receipt of the material.

(c) This offering will continue until terminated by the Secretary of the Treasury.

§ 344.1 General provisions.

(a) *Regulations.* United States Treasury securities —State and Local Government Series shall be subject to the general regulations with respect to United States securities, which are set forth in the Department of the Treasury Circular No. 300 (31 CFR part 306), to the extent applicable. Copies of the circular may be obtained from the Bureau of the Public Debt, Forms Management—Room 301, 200 Third Street, PO Box 396, Parkersburg, WV 26102–0396, or a Federal Reserve Bank or Branch.

(b) *Issuance.* The securities will be issued in book-entry form on the books of the Department of the Treasury, Bureau of the Public Debt, Parkersburg, WV 26102–0396. Transfer of securities by sale, exchange, assignment or pledge, or otherwise will not be permitted.

(c) *Transfers.* Securities held in an account of any one type, i.e., time deposit, demand deposit, or special zero interest, may not be transferred within that account or to an account of any other type.

(d) *Fiscal agents.* Selected Federal Reserve Banks and Branches, as fiscal agents of the United States, may be designated to perform such services as may be requested of them by the Secretary of the Treasury in connection with the purchase of, transactions involving, and redemption of, the securities.

(e) *Authority of subscriber.* Where a commercial bank submits an initial or final subscription on behalf of a government body, it must certify that it is acting under the latter's specific authorization; ordinarily, evidence of such authority will not be required. Subscriptions submitted by an agent other than a commercial bank must be accompanied by evidence of the agent's authority to act. Such evidence must describe the nature and scope of the agent's authorization, must specify the legal authority under which the agent was designated, and must relate by its terms to the investment action being undertaken. Subscriptions unsupported by such evidence will not be accepted.

(f) *Reservations.* Transaction requests, including requests for subscription and redemption, will not be accepted if unsigned, inappropriately completed, or not timely submitted. The Secretary of the Treasury reserves the right:

(1) To reject any application for the purchase of securities under this offering;

(2) To refuse to issue any such securities in any case or any class(es) of cases; and

(3) To revoke the issuance of any security, and to declare the subscriber ineligible thereafter to subscribe for securities under this offering, if any security is issued on the basis of an improper certification or other misrepresentation by the subscriber, other than as the result of an inadvertent error, if the Secretary deems such action to be in the public interest.

(4) Any of these actions shall be final. The authority of the Secretary to waive regulations under 31 CFR 306.126 applies to Part 344.

(g) *Debt limit contingency.* The Department of the Treasury reserves the right to change or suspend the terms and conditions of this offering, including provisions relating to subscriptions for, and issuance of, securities, interest payments, redemptions, and rollovers, as well as notices relating hereto, at any time the Secretary determines that issuance of obligations sufficient to conduct the orderly financing operations of the United States cannot be made without exceeding the statutory debt limit. Announcement of such changes shall be provided by such means as the Department deems appropriate.

(Approved by the Office of Management and Budget under control number 1535–0091)

Subpart B—Time Deposit Securities

§ 344.2 Description of securities.

(a) *Terms.*

(1) *Certificates of Indebtedness.* The certificates will be issued in a minimum amount of $1,000, or in any larger amount, in multiples of $100, with maturity periods fixed by the government body, from 30 calendar days up to and including one year, or for any intervening period.

(2) *Notes.* The notes will be issued in a minimum amount of $1,000, or in any larger amount, in multiples of $100, with maturity periods fixed by the government body, from one year and one day up to and including 10 years, or for any intervening period.

(3) *Bonds.* The bonds will be issued in a minimum amount of $1,000, or in any larger amount, in multiples of $100, with maturity periods fixed by the government body, from 10 years and one day up to and including 30 years, or for any intervening period.

(b) *Interest rate.* Each security shall bear such rate of interest as the government body shall designate, but the rate shall not exceed the maximum interest rate. The applicable maximum interest rates for each day shall equal rates shown in a table (Form PD 4262), which will be released to the public by 10:00 a.m., Eastern time, each business day. If the Treasury finds that due to circumstances beyond its control the rates will not be available to the public by 10:00 a.m., Eastern time, on any given business day, it will provide an immediate announcement of that fact and advise that the applicable interest for the last preceding business day shall apply. The applicable rate table for any subscription is the one in effect on the date the initial subscription is telecopied, if transmitted by facsimile equipment, postmarked, if mailed, or carrier date-stamped, if the initial subscription is delivered by other carrier. Subscriptions telecopied, postmarked, or date-stamped on a non-business day will be subject to those interest rates which are in effect for the next business day. The rates specified in the tables are one-eighth of one percent below the then current estimated Treasury borrowing rate for a security of comparable maturity.

(c) *Payment.*

(1) *Interest computation and payment dates.* Interest on a certificate will be computed on an annual basis and will be paid at maturity with the principal. Interest on a note or bond will be paid semiannually. The subscriber will specify the first interest payment date, which must occur any time between 30 days and one year of the date of issue,

and the final interest payment date must coincide with the maturity date of the security. Interest for other than a full semiannual interest period is computed on the basis of a 365-day or 366-day year (for certificates) and on the basis of the exact number of days in the half-year (for notes and bonds). See appendix to subpart E of part 306 of this chapter for rules regarding computation of interest.

(2) *Method of payment.* For securities for which subscriptions are submitted on or after February 1, 1987, payment will only be made by the Automated Clearing House method (ACH) for the owner's account at a financial institution designated by the owner. To the extent applicable, provisions of § 357.26 on ''Payments,'' as set forth in 31 CFR part 357 and provisions of 31 CFR part 370, shall govern ACH payments made under this offering. For securities for which subscriptions were submitted prior to February 1, 1987, payment will be made:

(i) By a direct credit to a Federal Reserve Bank or Branch for the account of the financial institution servicing the investor; or

(ii) By ACH for the owner's account at a financial institution; or

(iii) By fiscal agency check; or

(iv) In accordance with other prior arrangements made by the subscriber with the Bureau of the Public Debt.

§ 344.3 Subscription for purchase.

(a) *Subscription requirements.* Subscriptions for purchase of securities under this offering must be submitted to the Division of Special Investments, Bureau of the Public Debt, 200 Third Street, PO Box 396, Parkersburg, WV 26102–0396. Initial and final subscriptions may be submitted by facsimile equipment at (304) 480–6818, by mail, or by other carrier. All subscriptions submitted by mail, whether initial or final, should be sent by certified or registered mail.

(b) *Initial subscriptions.*

(1) An initial subscription, either on a designated Treasury form or in letter form, stating the principal amount to be invested and the issue date, must be telecopied, postmarked, or where delivered by other carrier, must be date-stamped at least 15 calendar days before issue date. For example, if the securities are to be issued on March 16, the subscription must be telecopied, postmarked, or date-stamped no later than March 1. If the initial subscription is in letter form, it should read substantially as follows:

To: Bureau of the Public Debt

____

Pursuant to the provisions of Department of the Treasury Circular, Public Debt Series No. 3–72, current revision, the undersigned hereby subscribes for United States Treasury Time Deposit Securities—State and Local Government Series, to be issued as entries on the books of the Bureau of the Public Debt, Department of the Treasury, in the total amount and with the issue date shown below, which date is at least 15 calendar days after the date of this subscription:

Principal Amount

$ ____

Issue Date

____

The undersigned agrees that the final subscription and payment will be submitted on or before the issue date.

____

(Tax I.D. Number of State or local government body or other entity eligible to purchase State and Local Government Series securities)

____

(Name of State or local government body or other entity eligible to purchase State and Local Government Series securities)

____

(Date)

by ____

(Signature and Title)

(2) The provisions set out in paragraph (e) of § 344.1, dealing with the authority of the subscriber to act on behalf of a government body, and in § 344.4, relating to the failure to complete a subscription, apply to initial, as well as final, subscriptions.

(3) An initial subscription may be amended on or before the issue date, but no later than 3:00 p.m., Eastern time, on the issue date. Notification may be telecopied by facsimile equipment to the Bureau of the Public Debt at (304) 480–6818 provided the request is clearly identified as an amendment and is immediately followed by the submission, by mail or other carrier, of written notification. Amendments to initial subscriptions are acceptable with the following exceptions:

(i) The issue date may not be changed to require issuance earlier than the issue date originally specified or to require issuance more than seven calendar days later than originally specified. If such change is made, notification should be provided to the Bureau of the Public Debt as soon as possible, but no later than 3:00 p.m., Eastern time, one business day before the originally specified issue date;

(ii) The aggregate amount may not be changed by more than the ten percent limitation set out in paragraph (c) of this section;

(iii) An interest rate may not be changed to a rate that exceeds the maximum interest rate in the table that was in effect on the date the initial subscription was submitted; and

(iv) Where an amendment is not submitted timely, the Division of Special Investments may determine, pursuant to the provisions governing waiver of regulations set forth under 31 CFR 306.126, that such an amendment is acceptable on an exception basis. Where an amendment is determined to be acceptable on an exception basis, the amended information shall be used as the basis for issuing the securities, and an administrative fee of $100 per subscription will be assessed. The Secretary reserves the right to reject amendments which are not submitted timely.

(4) No initial subscription will be required where a final subscription is received or postmarked at least 15 calendar days before the issue date. Such final subscription will be treated as the initial subscription for purposes of determining the applicable interest rate table (see § 344.2(b)), and may be amended on or before the issue date, subject to the exceptions in paragraph (b)(3) of this section.

(c) *Final subscriptions.* A final subscription must be received by the Bureau of the Public Debt on or before the issue date, but no later than 3:00 p.m., Eastern time, on the issue date. The final subscription may be telecopied by facsimile equipment to the Bureau of the Public Debt at (304) 480–6818, provided the facsimile is properly identified as a final subscription and is immediately followed by the submission of the original subscription form by mail or other carrier. The final subscription must be for a total principal amount that is no more than ten percent above or below the aggregate principal amount specified in the initial subscription. The final subscription, dated and signed by an official authorized to make the purchase and showing the taxpayer identification number of the beneficial owner, must be accompanied by a copy of the initial subscription, where applicable. The various maturities, interest rates, and semiannual interest payment dates (in the case of notes and bonds), must be specified in the final subscription, as well as the title(s) of the designated official(s) authorized to request early redemption. Final subscriptions submitted for certificates, notes and bonds must separately itemize securities of each maturity and each interest rate. The final subscription must contain a certification by the subscriber that, as of the date of investment (without regard to any temporary period of no longer than 30 days):

(1) The total investment consists only of proceeds (including amounts treated as proceeds) of a tax-exempt bond issue which are subject to yield restrictions under sections 141–150 of the Internal Revenue Code during the entire period of investment;

(2) The total investment is not less than all of such proceeds except for—

(i) An amount not to exceed $100, and

(ii) Amounts required for payment due less than 30 days from the date of issue;

(3) None of the proceeds submitted in payment is derived (directly or indirectly) from the redemption before maturity of other securities of the State and Local Government Series; and

(4) (i) No portion of the investment is being made (directly or indirectly) with amounts that are to be used to discharge a tax-exempt bond issue and that are derived or are to be derived (directly or indirectly) from the sale of escrowed open market securities, the proceeds of which were to be used to discharge a tax-exempt bond issue; or

(ii) Although a portion of the investment is being made (directly or indirectly) with amounts that are to be used to discharge a tax-exempt bond issue and that are derived or are to be derived (directly or indirectly) from the sale of escrowed open market securities, the proceeds of which were to be used to discharge a tax-exempt bond issue, the composite yield to maturity of all investments being purchased with such amounts does not exceed the composite yield to maturity of the securities that were sold, based on the price at which they were sold.

(5) Where proceeds are subject to yield restrictions for a limited period of time, under paragraph (c)(1) of this section, no investment of such proceeds beyond such period may be made. For example, if a reserve fund of a refunding issue is subject to yield restrictions for a period of four years, the securities purchased as an investment of the reserve fund may not have a maturity longer than four years. With respect to obligations described in section 103 of the Internal Revenue Code issued after January 31, 1987, paragraph (c)(2) of this section is satisfied only if on the date of investment, all the proceeds of the issue which are subject to yield restrictions are invested in State and Local Government Series securities. Paragraph (c)(2) of this section does not apply to purpose investments, such as mortgage notes or student loan obligations. Transferred proceeds of the tax exempt bond issue that were proceeds of another issue shall not be treated as proceeds for purposes of paragraph (c)(2) of this section if no portion of the total investment consists of such proceeds. See § 344.1(f) as to improper certifications.

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§ 344.4 Issue date and payment.

(a) *General.* The subscriber shall fix the issue date of each security in the initial subscription. The issue date must be a business day and may not exceed by more than 60 calendar days either the date the initial subscription was telecopied to the Bureau of the Public Debt or, where mailed, the postmark date, or where delivered by other carrier, the carrier date-stamp thereof. Full payment for each subscription must be submitted by the Fedwire funds transfer system with credit directed to the Treasury's General Account. Full payment should be submitted by 3:00 p.m., Eastern time, to ensure that settlement on the securities occurs on the date of issue.

(b) *Noncompliance.* The penalty imposed on any subscriber which fails to make settlement on a subscription once submitted shall be to render the subscriber ineligible thereafter to subscribe for securities under this offering for a period of six months, beginning on the date the subscription is withdrawn or the proposed issue date, whichever occurs first. The Division of Special Investments may determine to waive the six month penalty, pursuant to the provisions governing waiver of regulations set forth under 31 CFR 306.126. Where settlement occurs after the proposed issue date and the Division of Special Investments determines, pursuant to 31 CFR 306.126, that settlement is acceptable on an exception basis, the six month penalty will be waived, and the subscriber shall be subject to a late payment assessment. The assessment will include payment of an amount equal to the amount of interest that would have accrued on the securities from the proposed issue date to the date of settlement, as well as an administrative fee of $100 per subscription. Assessments under this subsection are due on demand. Failure to pay an assessment shall render the subscriber ineligible thereafter to subscribe for securities under this offering until the assessment is paid.

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§ 344.5 Redemption.

(a) *General.* A security may not be called for redemption by the Secretary of the Treasury prior to maturity. Upon the maturity of a security, the Department will make payment of the principal amount and interest due to the owner thereof. A security scheduled for redemption on a non-business day will be redeemed on the next business day.

(b) *Before maturity.*

(1) *In general.* A security may be redeemed at the owner's option no earlier than 25 calendar days after the issue date in the case of a certificate, and one year after the issue date in the case of a note or bond. Partial redemptions may be requested in multiples of $100; however, an account balance of less than $1,000 will be redeemed in total.

(2) *Notice.* Notice of redemption prior to maturity must be submitted, either on a designated Treasury form or by letter, by the official(s) authorized to redeem the securities, as shown on the final subscription form, to the Division of Special Investments, Bureau of the Public Debt, 200 Third Street, PO Box 396, Parkersburg, WV 26102–0396. The notice may be submitted by facsimile equipment to the Bureau of the Public Debt at (304) 480–6818, by mail, or by other carrier. The notice must show the account number, the maturities of the securities to be redeemed, and the tax identification number of the subscriber. The notice of redemption must be telecopied, postmarked, or where delivered by other carrier, must be date-stamped no less than 15 calendar days before the requested redemption date, but no more than 60 calendar days before the requested redemption date. A notice of redemption prior to maturity may not be cancelled.

(3) *Redemption proceeds—Subscriptions on or after September 1, 1989.* For securities subscribed for on or after September 1, 1989, the amount of the redemption proceeds is calculated as follows:

(i) *Interest.* If a security is redeemed before maturity on a date other than a scheduled interest payment date, interest will be paid for the fractional interest period since the last interest payment date.

(ii) *Market charge.* An amount shall be deducted from the redemption proceeds in all cases where the current borrowing rate of the Department of the Treasury for the remaining period to original maturity of the security prematurely redeemed exceeds the rate of interest originally fixed for such security. The amount shall be the present value of the future increased borrowing cost to the Treasury. The annual increased borrowing cost for each interest period is determined by multiplying the principal by the difference between the two rates. For notes and bonds, the increased borrowing cost for each remaining interest period to original maturity is determined by dividing the annual cost by two. For certificates, the increased borrowing cost for the remaining period to original maturity is determined by multiplying the annual cost by the number of days remaining until original maturity divided by the number of days in the calendar year. Present value shall be determined by using the current borrowing rate as the discount factor. The term ''current borrowing rate'' means the applicable rate shown in the table of maximum interest rates payable on United States Treasury securities—State and Local Government Series—for the day the request for early redemption is telecopied, postmarked, or where delivered by other carrier, date-stamped, plus one-eighth of one percentage point. Where redemption is requested as of a date less than 30 calendar days before the original maturity date, such applicable rate is the rate shown for a security with a maturity of 30 days. The market charge for bonds, notes, and certificates of indebtedness can be computed by use of the formulas in Appendix A to this part.

(4) *Redemption proceeds—Subscriptions from December 28, 1976 through August 31, 1989.* For securities subscribed for from December 28, 1976 through August 31, 1989, the amount of the redemption proceeds is calculated as follows:

(i) *Interest.* Interest for the entire period the security was outstanding shall be recalculated on the basis of the lesser of the original interest rate at which the security was issued, or the interest rate that would have been set at the time of the initial subscription had the term for the security been for the shorter period. If a note or bond is redeemed before maturity on a date other than a scheduled interest payment date, no interest will be paid for the fractional interest period since the last interest payment date.

(ii) *Overpayment of interest.* If there have been overpayments of interest, as determined under paragraph (b)(4)(i) of this section, there shall be deducted from the redemption proceeds the aggregate amount of such overpayments, plus interest, compounded semiannually, thereon from the date of each overpayment to the date of redemption. The interest rate to be used in calculating the interest on the overpayment shall be one-eighth of one percent above the maximum rate that would have applied to the initial subscription had the term of the security been for the shorter period.

(iii) *Market charge.* An amount shall be deducted from the redemption proceeds in all cases where the current borrowing rate of the Department of the Treasury for the remaining period to original maturity of the security prematurely redeemed exceeds the rate of interest originally fixed for such security. The amount shall be calculated using the formula in paragraph (b)(3)(ii) of this section.

(5) *Redemption proceeds—Subscriptions on or before December 27, 1976.*

(i) For securities subscribed for on or before December 27, 1976, the amount of the redemption proceeds is calculated as follows.

(ii) The interest for the entire period the security was outstanding shall be recalculated on the basis of the lesser of the original interest rate at which the security was issued, or an adjusted interest rate reflecting both the shorter period during which the security was actually outstanding and a penalty. The adjusted interest rate is the Treasury rate which would have been in effect on the date of issuance for a marketable Treasury certificate, note, or bond maturing on the quarterly maturity date prior to redemption (in the case of certificates), or on the semiannual maturity period prior to redemption (in the case of notes and bonds), reduced in either case by a penalty which shall be the lesser of:

(A) One-eighth of one percent times the number of months from the date of issuance to original maturity, divided by the number of full months elapsed from the date of issue to redemption, or

(B) One-fourth of one percent.

There shall be deducted from the redemption proceeds, if necessary, any overpayment of interest resulting from previous payments made at a higher rate based on the original longer period to maturity.

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Subpart C—Demand Deposit Securities

§ 344.6 Description of securities.

(a) *Terms.* The securities are defined as one-day certificates of indebtedness. The securities will be issued in a minimum of $1,000 and any increment above that amount. Each subscription will be established as a unique account. Securities will be automatically rolled over each day unless redemption is requested.

(b) *Interest rate.*

(1) Each security shall bear a variable rate of interest based on an adjustment of the average yield for three-month Treasury bills at the most recent auction. A new rate will be effective on the first business day following the regular auction of three-month Treasury bills and will be shown in the table (Form PD 4262), available to the public on such business day. Interest will be accrued and added to principal daily. Interest will be computed on the balance of the principal, plus interest accrued through the immediately preceding day.

(2) (i) The annualized effective demand deposit rate in decimals, designated ''I'' in Equation 1 is calculated as:

$$I=[(100/P)^{Y/DTM}-1](1-MTR)-TAC$$

(Equation 1)

where

P=The average auction price for the Treasury bill, per hundred, to three decimal places.

Y=365 if the year following issue date does not contain a leap year day and 366 if it does contain a leap year day.

DTM=The number of days from date of issue to maturity for the auctioned Treasury bill.

MTR=Estimated average marginal tax rate, in decimals, of purchasers of short-term tax exempt bonds.

TAC=Treasury administrative costs, in decimals.

(ii) The daily factor for the demand deposit rate is then calculated as:

$$DDR=(1+I)^{1/Y}-1$$

(Equation 2)

(3) Information as to the estimated average marginal tax rate and costs for administering the demand deposit State and Local Government Series securities program, both to be determined by Treasury from time to time, will be published in the **Federal Register**.

(c) *Payment.* Interest earned on the securities will be added to the principal and will be reinvested daily until redemption. At any time the Secretary determines that issuance of obligations sufficient to conduct the orderly financing operations of the United States cannot be made without exceeding the statutory debt limit, the Department will invest any unredeemed demand deposit securities in special 90-day certificates of indebtedness. These 90-day certificates will be payable at maturity, but redeemable before maturity, provided funds are available for redemption, or reinvested in demand deposit securities when regular Treasury borrowing operations resume, both at the owner's option. Funds invested in the 90-day certificates of indebtedness will earn simple interest equal to the daily factor in effect at the time demand deposit security issuance is suspended, multiplied by the number of days outstanding.

§ 344.7 Subscription for purchase.

(a) *Subscription requirements.* Subscriptions for purchase of securities under this offering must be submitted to the Division of Special Investments, Bureau of the Public Debt, 200 Third Street, PO Box 396, Parkersburg, WV 26102–0396. Subscriptions must be submitted on a designated Treasury form, must specify the principal amount to be invested and the issue date, and must be signed by an official authorized to make the purchase. The Bureau of the Public Debt must receive the subscription at least three business days before the issue date. The subscription may be submitted by certified or registered mail, or by other carrier. The subscription may also be submitted by facsimile equipment at (304) 480–6818, at least three business days before the issue date, provided that the original subscription form is submitted by mail, or by other carrier, and is received by the Division of Special Investments by 3:00 p.m., Eastern time, on the issue date.

(b) *Amending subscriptions.* The principal amount to be invested may be changed without penalty on or before the issue date, but no later than 1:00 p.m. Eastern time, on the issue date. Notification may be telecopied by facsimile equipment to the Division of Special Investments at (304) 480–6818, provided the request is clearly identified as an amendment and is immediately followed by the submission, by mail or other carrier, of written notification. Where an amendment is not submitted timely, the Division of Special Investments may determine, pursuant to the provisions governing waiver of regulations set forth under 31 CFR 306.126, that such an amendment is acceptable on an exception basis. Where an amendment is determined to be acceptable on an exception basis, the amended information shall be used as the basis for issuing the securities, and an administrative fee of $100 per subscription will be assessed. The Secretary reserves the right to reject amendments which are not submitted timely.

(c) *Certification.* By completing the subscription form, subscribers certify to the following:

(1) Neither the aggregate issue price nor the stated redemption price at maturity of the bonds that are part of the tax-exempt issue exceeds $35 million. Issue price and stated redemption price at maturity have the meanings given such terms in sections 1273 and 1274 of the Internal Revenue Code;

(2) No portion of the tax-exempt bond issue has been or will be issued or permitted to remain outstanding, and the expenditure of gross proceeds of the tax-exempt bond issue has not and will not be delayed, for the principal purpose of investing in demand deposit securities;

(3) Only eligible gross proceeds of the tax-exempt bond issue have been and will be submitted in payment for demand deposit securities. Eligible gross proceeds are all gross proceeds of the tax-exempt bond issue except—

(i) Gross proceeds of an advance refunding issue to be used to discharge another issue;

(ii) Gross proceeds accumulated in a reserve or replacement fund (other than a bona fide debt service or reasonably required reserve or replacement fund); and

(iii) Solely for purposes of this paragraph (c)(3), gross proceeds previously invested at any time pursuant to any exception in paragraph (c)(5) of this section, other than paragraph (c)(5)(vi) (Exception 6) (relating to amounts of less than $25,000) and paragraph (c)(5)(viii) (Exception 8) (relating to inadvertent error).

(4) At least 25 percent of the eligible gross proceeds received from the sale of the tax-exempt bond issue have been or will be invested in demand deposit securities within three business days of the date of receipt thereof;

(5) All eligible gross proceeds of the tax-exempt bond issue have been and will be invested within four business days of the date of receipt thereof in demand deposit securities (principal repayments on purpose investments are treated as gross proceeds received on the date of repayment). This paragraph (c)(5) shall not apply to gross proceeds that are at all times (prior to the date of expenditure thereof) invested pursuant to one of the exceptions:

(i) *Exception 1.* Gross proceeds that are invested solely in investments the earnings on which are not subject to rebate under section 143(g)(3) or 148(f) of the Internal Revenue Code (whichever applies).

(ii) *Exception 2.* Gross proceeds that are invested in obligations the earnings on which are not reasonably expected to be subject to rebate by reason of section 148(f)(4)(A)(ii) (relating to certain bona fide debt service funds) of the Internal Revenue Code or section 148(f)(4)(B) (relating to exception for temporary investments) of the Internal Revenue Code.

(iii) *Exception 3.* Gross proceeds that are not reasonably expected to be gross proceeds of the tax-exempt bond issue for more than seven business days.

(iv) *Exception 4.* Gross proceeds that are part of a reasonably required reserve or replacement fund (other than a bona fide debt service fund) for the tax-exempt bond issue.

(v) *Exception 5.* Gross proceeds that are invested in taxable obligations, but only if the yield on each obligation (computed separately and on the basis of an arm's length purchase price) is no higher than the yield on the tax-exempt bond issue.

(vi) *Exception 6.* Eligible gross proceeds that are not invested in one-day certificates of indebtedness or pursuant to paragraphs (c)(5)(i)–(v) (Exceptions 1 through 5), but only if the total amount of such eligible gross proceeds on any particular day is less than $25,000. This paragraph (c)(5)(vi) (Exception 6) shall not apply to gross proceeds that are part of a reasonably required reserve or replacement fund (other than a bona fide debt service fund).

(vii) *Exception 7.* Gross proceeds that are not invested pursuant to paragraph (c)(5)(iv) (Exception 4) or paragraph (c)(5)(vi) (Exception 6), and that are invested in any taxable obligation the yield on which is higher than the yield on the tax-exempt bond issue, but only if taxable obligations described in paragraph (c)(5)(v) (Exception 5), and the tax-exempt obligations described in (c)(5)(i) (Exception 1) are not available for investment (for example, because market interest rates are too high and statutory or indenture restrictions prevent investments in tax-exempt obligations).

(viii) *Exception 8.* Gross proceeds that are not invested in demand deposit securities due to an inadvertent error.

(6) See § 344.1(f) as to improper certifications.

§ 344.8 Issue date and payment.

(a) *General.* The subscriber shall fix the issue date on the subscription, the issue date to be a business day at least three business days after receipt of the subscription by the Division of Special Investments. Full payment for each subscription must be submitted by the Fedwire funds transfer system with credit directed to the Treasury's General Account. Full payment should be submitted by 3:00 p.m., Eastern time, to ensure that settlement on the securities occurs on the date of issue.

(b) *Noncompliance.* The penalty imposed on any subscriber which fails to make settlement on a subscription once submitted shall be to render the subscriber ineligible thereafter to subscribe for securities under this offering for a period of six months, beginning on the date the subscription is withdrawn or the proposed issue date, whichever occurs first. The Division of Special Investments may determine to waive the six month penalty, pursuant to the provisions governing waiver of regulations set forth under 31 CFR 306.126. Where settlement occurs after the proposed issue date and the Division of Special Investments determines, pursuant to 31 CFR 306.126, that settlement is acceptable on an exception basis, the six month penalty will be waived, and the subscriber shall be subject to a late payment assessment. The assessment will include payment of an amount equal to the amount of interest that would have accrued on the securities from the proposed issue date to the date of settlement, as well as an administrative fee of $100 per subscription. Assessments under this subsection are due on demand. Failure to pay an assessment shall render the subscriber ineligible thereafter to subscribe for securities under this offering until the assessment is paid.

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§ 344.9 Redemption.

(a) *General.* A security may be redeemed at the owner's option, provided a request for redemption is received not less than one business day prior to the requested redemption date. Partial redemptions may be requested; however, an account balance of less than $1,000 will be redeemed in total. Payment will be made by crediting the reserve account maintained at the Federal Reserve Bank or Branch by the financial institution servicing the account owner.

(b) *Notice.* Notice of redemption must be submitted, either on a designated Treasury form or by letter, by the official(s) authorized to redeem the securities, as shown on the subscription form, to the Division of Special Investments, Bureau of the Public Debt, 200 Third Street, PO Box 396, Parkersburg, WV 26102–0396. The notice may be submitted by facsimile equipment to the Bureau of the Public Debt at (304) 480–6818, by mail, or by other carrier. The notice must show the account number and the tax identification number of the subscriber. The notice of redemption must be received at the Bureau of the Public Debt by 1:00 p.m., Eastern time, one business day prior to the requested redemption date.

(c) *Certification.* By completing the redemption form, subscribers certify to the fact that the proceeds to be received will be expended within one day of receipt thereof for the purpose for which the tax-exempt bond was issued.

Subpart D—Special Zero Interest Securities

§ 344.10 General.

Provisions of subpart B of this part (Time Deposit Securities) apply except as specified in subpart D of this part.

§ 344.11 Description of securities.

(a) *Terms.* Only certificates of indebtedness and notes are offered.

(1) *Certificates of Indebtedness.* The certificates will be issued in a minimum amount of $1,000, or in any larger amount, in multiples of $100, with maturity periods fixed by the government body, from 30 calendar days up to and including one year, or for any intervening period.

(2) *Notes.* The notes will be issued in a minimum amount of $1,000, or in any larger amount, in multiples of $100, with maturity periods fixed by the government body, from one year and one day up to and including 10 years, or for any intervening period.

(b) *Interest rate.* Each security shall bear no interest.

§ 344.12 Subscription for purchase.

In lieu of the certification under § 344.3(c), the final subscription must contain a certification by the subscriber that:

(a) The total investment consists only of original or investment proceeds of a tax-exempt bond issue that are subject to yield restrictions under sections 141–150 of the Internal Revenue Code;

(b) None of the original proceeds of the tax-exempt bond issue were subject to arbitrage yield restrictions under section 148 of the Internal Revenue Code on the date of receipt thereof; and

(c) None of the proceeds submitted in payment are proceeds of an advance refunding issue to be used to discharge another issue or part of a reserve or replacement fund for the advance refunding issue.

§ 344.13 Redemption.

(a) *General.* Provisions of § 344.5(a) apply.

(b) *Before maturity.*

(1) *In general.* A security may be redeemed at the owner's option no earlier than 25 calendar days after the issue date in the case of a certificate and one year after the issue date in the case of a note. No market charge or penalty shall apply in the case of the redemption of a special zero interest security before maturity.

(2) *Notice.* Notice of redemption prior to maturity must be submitted, either on a designated Treasury form or by letter, by the official(s) authorized to redeem the securities, as shown on the final subscription form, to the Division of Special Investments, Bureau of the Public Debt, 200 Third Street, PO Box 396, Parkersburg, WV 26102–0396. The notice may be submitted by facsimile equipment to the Bureau of the Public Debt at (304) 480–6818, by mail, or by other carrier. The notice must show the account number, the maturities of the securities to be redeemed, and the tax identification number of the subscriber. The notice of redemption must be telecopied, postmarked, or where delivered by other carrier, must be date-stamped no less than 15 calendar days before the requested redemption date, but no more than 60 calendar days before the requested redemption date. A notice of redemption prior to maturity cannot be cancelled.

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Appendix A to Part 344—Early Redemption Market Change Formulas and Examples

A. The amount of the market charge for bonds and notes can be determined through use of the following formula:

$$M = \frac{\left(\frac{b}{2}\right)\left(\frac{r}{s}\right) + \frac{b}{2}(a)}{1 + \left(\frac{r}{s}\right)\left(\frac{i}{2}\right)}$$

where

M=market charge

b=increased annual borrowing cost (i.e., principal multiplied by the excess of the current borrowing rate for the period from redemption to original maturity of note or bond over the rate for the security)

r=number of days from redemption to beginning of next semiannual interest period

s=number of days in current semiannual period

i=current borrowing rate for period from redemption to maturity (expressed in decimals)

n=number of remaining full semiannual periods to the original maturity date

$$a = \frac{\left(1 - v^n\right)}{\frac{i}{2}} \qquad \text{(Equation 2)}$$

$$v^n = \frac{1}{\left(1+\frac{i}{2}\right)^n} \quad \text{(Equation 3)}$$

B. The application of this formula may be illustrated by the following example:

(1) Assume that a $600,000 note is issued on July 1, 1985, to mature on July 1, 1995. Interest is payable at a rate of 8% on January 1 and July 1.

(2) Assume that the note is redeemed on February 1, 1989, and that the current borrowing rate for Treasury at that time for the remaining period of 6 years and 150 days is 11%.

(3) The increased annual borrowing cost is $18,000. ($600,000)×(11%−8%)

(4) The market charge is computed as follows:

$$M = \frac{\left(\frac{\$18,000}{2}\right)\left(\frac{150}{181}\right)+\left(\frac{\$18,000}{2}\right)(a)}{1+\left(\frac{150}{181}\right)\left(\frac{.11}{2}\right)} =$$

$$\frac{\$7,458.56+(\$9,000)(a)}{1.045580111} = \quad \text{(Equation 5)}$$

$$\frac{\$7,458.56+(\$9,000)\left(\frac{1-\frac{1}{(1+\frac{.11}{2})^{12}}}{\frac{.11}{2}}\right)}{1.045580111} = \quad \text{(Equation 6)}$$

$$\frac{\$7,458.56+(\$9,000)(8.618517849)}{1.045580111} = \quad \text{(Equation 7)}$$

$$\frac{\$7,458.56+\$77,566.66}{1.045580111} = \quad \text{(Equation 8)}$$

$81,318.71

(Equation 9)

C. The amount of the market charge for certificates can be determined through use of the following formula:

$$M = \frac{(b)\left(\frac{r}{s}\right)}{1+\frac{r}{s}(i)} \quad \text{(Equation 10)}$$

where

M=market charge

b=increased borrowing cost for full period

r=number of days from redemption date to original maturity date

s=number of days in current annual period (365 or 366)

i=current borrowing rate expressed in decimals (discount factor)

D. The application of this formula may be illustrated by the following example:

(1) Assume that a $50,000 certificate is issued on March 1, 1987, to mature on November 1, 1987. Interest is payable at a rate of 10%.

(2) Assume that the certificate is redeemed on July 1, 1987, and that the current borrowing cost to Treasury for the 123-day period from July 1, 1987, to November 1, 1987, is 11.8%.

(3) The increased annual borrowing cost is $900. ($50,000−11.8%−10%)

(4) The market charge is computed as follows:

$$M = \frac{\$900\left(\frac{123}{365}\right)}{1+\left(\frac{123}{365}\right)(.118)} = \quad \text{(Equation 11)}$$

$$\frac{303.29}{1.039764384} = \quad \text{(Equation 12)}$$

$291.69

(Equation 13)

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