requirement could be burdensome for entities that do not have systems for electronic recordkeeping.

III. Section-by-Section Analysis of Proposed Regulations

A. Section 400.1. Scope of Regulations

A new paragraph is proposed to be added to Part 400 to describe the statutory basis for the large position rules. The paragraph also states that the large position rules are located in Part 420.

B. Part 420. Large Position Reporting

1. Section 420.1

Applicability. This section sets out the scope of the large position recordkeeping and reporting rules by identifying the types of Treasury securities covered and by defining the universe of entities potentially affected. Section 420.1 reflects the Department's initial determination that all marketable Treasury securities—bills, notes and bonds—should be included within the scope of the rules. However, arguments have been made that features and characteristics of the bill market, such as the frequency of issues (i.e., weekly) and reopenings, the size of bill auctions and the availability of several instruments that are close substitutes for bills (e.g., various money market instruments), make it more difficult to accumulate concentrations of ownership of Treasury bills. Comments are specifically requested on whether Treasury bills should be included in the large position recordkeeping and reporting rules.

On its face, part 420 applies to any type of entity, foreign or domestic, that might control a large position in a specific Treasury security. This broad construct of potential application is consistent with the statutory purpose: ''Large position reporting also would be useful in assuring that regulators can monitor the positions of major market participants other than government securities brokers or dealers under certain circumstances. In particular, it will provide assurance that the government can compel disclosure of position information when necessary from all large market participants, including a group of relatively unregulated entities called 'hedge funds.' '' [15] As described in the preamble discussion of sections 420.3 and 420.4, the number of entities that may actually be affected by large position rules is significantly narrowed when the minimum size for a large position is applied.

We believe it is appropriate to exclude certain entities from the application of the rules based on the existing availability of position information on these organizations and/or concerns about the confidentiality of this information. Accordingly, paragraphs (b) and (c) of section 420.1 provide exemptions from part 420 to the holdings of foreign central banks, foreign governments, international monetary authorities and Federal Reserve Banks (FRBs). The exemptions for the foreign entities are limited to their respective positions maintained at the FRBNY. The exemptions are also consistent with the position expressed by the Senate and House during consideration of the legislation.[16]

One commenter, responding to the ANPR, expressed concern about granting exemptions specifically to these foreign entities. However, the Department believes the proposed approach is appropriate since the exemptions are limited in their scope by applying only to the portion of the organization's position that is maintained at the FRBNY. Any positions held by the exempt entities at locations other than the FRBNY are not exempted and will be subject to the large position recordkeeping and reporting rules. The proposed exemption for those Treasury securities that FRBs hold and control for their own accounts is also based on the Department's access to this information.

The Department recognizes that on rare occasions it may be necessary to request large position information on Treasury securities that are not within the parameters of the proposed definition of recently-issued (paragraph 420.2(g)) but that are within the scope of the intent of the statute. For example, in August 1991, Treasury might have sought large position information on the April 1991 two-year note, given that the security was still ''on special'' in the repurchase agreement market and there was a significant concentration of ownership. While this security, at that time, would have been outside the scope of the currently proposed definition, the Department believes it is necessary to reserve the right to collect large position information in such circumstances. Accordingly, we have included within the rule a reservation to request information on additional Treasury security issues consistent with the purposes of the GSAA.

2. Section 420.2

Definitions. This section provides for the definitions of terms that are integral to the large position rules. Unless otherwise defined in this section, terms used in part 420 have the same meanings provided in section 400.3.

''Control''—The concept of control revolves around three elements: beneficial ownership, possession (custody) and investment discretion. The beneficial owner is the party with the actual ownership interest in the Treasury security. The beneficial owner may or may not always be aware of its ownership position in a given security if it does not manage its own investments and it may not have possession of the Treasury securities even if it makes its own investment decisions (especially likely with book-entry Treasury securities). Possession or custody is evidenced by an organization's ability to service the securities directly (e.g., transfer the securities, receive interest and principal payments). The beneficial owner may perform this function for its own holdings, but the mechanics of book-entry Treasury securities require that a depositary institution act in this capacity on behalf of others at some level in the custody chain for all Treasury securities. Additionally, book-entry Treasury securities may involve more than one custodian in the holding of a specific security entitlement.[17] Investment discretion is the authority to make and execute decisions about the purchase, sale and retention of securities. In the institutional market for Treasury securities, which is of critical importance in developing large position reporting rules, the granting of investment discretion to an investment adviser to manage all or some portion of an entity's portfolio is common.

It is our view that, for the purposes of large position reporting, the most important criterion in the definition of control is that of investment discretion. While beneficial owners receive the economic benefit of holding a Treasury security, frequently, they do not make the decision to purchase/sell/retain the Treasury security and, as mentioned, may not, on a day to day basis, be aware

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[15] H.R. Rep. 103–255, September 23, 1993, at pg. 25.

[16] 139 Cong. Rec. H–10967 (daily ed. November 22, 1993) Statement of Chairman Dingell on S. 422.

[17] The Federal Reserve Banks maintain book-entry security accounts for depository institutions and other entities such as government and international agencies and certain foreign central banks. In their book-entry accounts at the Federal Reserve, the depository institutions may maintain their own security holdings and holdings for customers, which may include other depository institutions, dealers, brokers, institutional investors and individuals. In turn, the depository institution's customers may maintain accounts for their customers. This creates a tiered chain of custodial relationships.