

FOR YOUR INFORMATION

SEC Issues No-Action Letter On Haircuts For Mortgage-Backed Securities

In December 1996, the Securities and Exchange Commission (SEC) Division of Market Regulation issued a no-action letter that allows broker/dealers to use the alternative method in the Net Capital Rule (SEC Rule 15c3-1) when calculating proprietary haircut charges on certain pass-through mortgage-backed securities sponsored by U.S. government agencies. The letter also addresses charges for these securities under various hedging scenarios.

The alternative method uses the relationship between a security's market price and its par value to determine the maturity of the security for computing net capital net haircuts under SEC Rule 15c3-1(c)(2)(vi)(A). It is based on the theory that "a mortgage-backed security with a high coupon rate will experience a significant amount of prepayment of principal and, consequently, will tend to have a short duration." As an example, the letter cites that "a thirty-year mortgage-backed security trading at \$108 with a par value of \$100 generally has a duration equal to a government security with nine to twelve months remaining maturity."

Members should note that, if they choose to use this alternative method, they must apply the alternative method to all pass-through mortgage-backed securities covered under the no-action letter. These include any security sponsored by a U.S. government agency that represents a pro rata interest or participation in the principal and interest cash flows generated by a pool of mortgage loans of which at least 95 percent of the aggregate principal is composed of fixed-rate residential mortgage loans on one-to-four family homes, including five- and seven-year mortgage loans with balloon payments at maturity. The letter

excludes multifamily, adjustable-rate, commercial, and mobile-home mortgage loans.

Members intending to apply these haircuts to pass-through mortgage-backed securities in their proprietary and other accounts should read the SEC's letter in its entirety. Requests for copies of the letter may be directed to Samuel L. Luque, Jr., Associate Director, Compliance Department, NASD Regulation, at (202) 728-8472; or Robert Broughton, District Coordinator, NASD Regulation, at (202) 728-8361.

West Virginia Securities Commission Increases Registration, Re-Registration, And Renewal Fees

Effective July 10, 1997, the West Virginia Securities Commission will increase its agent registration and agent re-registration fee to \$80. In addition, effective with the 1997-98 renewal program, West Virginia's agent renewal fee will increase to \$65.

If you have any questions regarding these changes, please contact your assigned Quality & Service Team or Gateway at (301) 590-6500.

SEC Approves Rule Permitting Electronic Submission Of Information

On May 9, 1997, the SEC approved a rule amendment that will allow the NASD[®] to request that members provide regulatory information in electronic form and to establish electronic submission programs for regularly filed regulatory information.

The rule that was amended requires members to submit oral or written reports in response to NASD requests for investigatory information. The amendment will provide that a member that maintains information in an electronic format may

be required to submit investigatory reports to the NASD electronically. The rule amendment also provides the NASD with authority to establish programs for the electronic submission of regularly filed information, with the approval of the SEC.

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