N.Y. STOCK EXCHANGE

INFORMATION MEMO

New York Stock Exchange, Inc.
55 Water Street
New York, New York 10041

Regulation and Surveillance

Number 80-66
December 31, 1980

ATTENTION: CHIEF FINANCIAL OFFICER/PARTNER

TO: Members and Member Organizations

SUBJECT: Amendments to Rule 328 (Sale-And-Leasebacks, Factoring, Financing and Similar Arrangements)

The SEC recently approved amendments to NYSE Rule 328 which require the following:

1) that any loan agreement, the proceeds of which are intended to reduce the deduction in computing net capital for fixed assets and assets which cannot be readily converted into cash under SEC Rule 15c3-1(c)(2)(iv), must be submitted to and be acceptable to the Exchange prior to such reduction becoming effective.

2) that any agreement relating to a determination of a "ready market" for securities based upon the securities being accepted as collateral for a loan by a bank under SEC Rule 15c3-1(c)(11)(ii) must be submitted to and be acceptable to the Exchange before the securities are deemed to have a "ready market."

Therefore, all new agreements executed on or subsequent to January 5, 1981 must be submitted to the Exchange for approval.

The principal purpose in reviewing such agreements is to determine whether the liabilities representing the loans must be considered as scheduled capital withdrawals under Rule 326.

The Uniform Net Capital Rule (SEC Rule 15c3-1) disallows value for assets not readily convertible into cash. However, there are two provisions under which value is allowed when such assets are pledged as collateral for a loan. When net capital value has been included under either provision, payment of the loan would have the same effect as a capital withdrawal.

Under one provision, (subparagraph (c)(2)(iv)), it is possible for a broker/dealer to increase net capital through borrowings or a chattel mortgage secured by the pledge of assets that are ordinarily deducted in computing net capital. This is illustrated through the following net capital computations:

	Before Loan	After Loan
Assets		
Cash in banks	$ 10,000	$ 60,000
Common stocks	200,000	200,000
Furniture and fixtures (or other non-allowable assets)	100,000	100,000
Total Assets	$310,000	$360,000
Liabilities		
Miscellaneous	$100,000	$100,000
Loan secured by pledge of furniture and fixtures		50,000
Total Liabilities	$100,000	$150,000
Net Worth	$210,000	$210,000
Net Capital Deductions		
Securities haircuts	$ 60,000	$ 60,000
Furniture and fixtures	100,000	50,000
Total deductions	$160,000	$110,000
Net Capital	$ 50,000	$100,000

This provision applies only to fixed liabilities adequately secured either:

- by assets acquired for use in the ordinary course of the broker/dealer's trade or business, or
- by any other asset, if the creditor's sole recourse for non-payment is to the asset pledged.

Under another provision, (subparagraph (c)(11)(ii)), value may be allowed for otherwise non-marketable securities up to the amount of adequately secured bank loans collateralized thereby.

Generally, if payment of the liability under any of the above provisions could be required by the lender on demand or is expected to be made in less than six months, it shall be considered a scheduled capital withdrawal to be included in a member organization's 326 ratio and reported as such in all FOCUS report submissions. Specifically it should be reported in Part I Item 4699 (now in use), Part I Item 4880 of new Part I to be issued shortly, Part II, page 11 -- Item 4870; or for those firms filing Part IIA, page 7.

In order for such liabilities not to be considered as scheduled capital withdrawals under Rule 326, the agreements covering the loans must meet certain standards relating to any provisions which would accelerate maturity, including events of default. Generally speaking, acceptable acceleration provisions would be treated in the same manner as an "Event of Acceleration" and an "Event of Default" as defined and interpreted pursuant to SEC Rule 15c3-1, Appendix D.

The agreements generally would have to meet at least the following standards:

1. Only those events which would be Events of Default in the standard subordination forms could cause the loan to be immediately due and payable.

2. Other events which could accelerate the maturity of the loan may do so only after a six month time period has run. As an example, a garnishment notice or lien levy in connection with an action brought by a third party may be considered an Event of Acceleration and our requirements relating to an Event of Acceleration shall apply.

3. Agreements must include a provision to the effect that any prepayment must have the prior approval of the Exchange.

4. Where appropriate, the lender must agree to rent the assets for at least 30 days to a trustee or liquidator in the "Event of Default".

5. A "no right of offset" provision must be included in each agreement. However, an agreement may contain a "right of offset" provision tied to at least a six month time delay upon an Event of Acceleration or upon an Event of Default tied to at least a 30 day time delay.

6. In order for a loan to be considered a sole recourse or a non-recourse loan, the agreement must include specific language to that effect. The inclusion of the "no right of offset" provision does <u>not</u> make it a sole recourse or a non-recourse loan.

7. Agreements must provide for immediate written notice to the Exchange in the event of <u>any</u> acceleration.

8. Agreements must have a fixed maturity date for a period in excess of six months.

A copy of Rule 328 as amended is attached.

Please refer questions on this matter to J. Leslie Daniels (212) 623-8462 or to your Supervising Coordinator.

Robert M. Bishop
Senior Vice President

ATTACHMENT

New language underscored

SALE-AND-LEASEBACKS, FACTORING, FINANCING AND SIMILAR ARRANGEMENTS

Rule 328(a) No member or member organization shall consummate a sale-and-lease-back arrangement with respect to any of its assets; a sale, factoring or financing arrangement with respect to any unsecured accounts receivable; or a sale or factoring arrangement with respect to any customers' debit balances without the prior written authorization of the Exchange.

(b) Any loan agreement the proceeds of which is intended to reduce the deduction in computing net capital for fixed assets and assets which cannot be readily converted into cash under SEC Rule 15c3-1(c)(2)(iv), must be submitted to and be acceptable to the Exchange prior to such reduction becoming effective.

(c) Any agreement relating to a determination of a "ready market" for securities based upon the securities being accepted as collateral for a loan by a bank under SEC Rule 15c3-1(c)(11)(ii) must be submitted to and be acceptable to the Exchange before the securities are deemed to have a "ready market."

CAPITAL REQUIREMENTS FOR INDIVIDUAL MEMBERS AND MEMBER ORGANIZATIONS

Rule 325

(d) The Exchange may at any time or from time to time with respect to a particular member or member organization or all members or member organizations or a new member or member organization require greater net capital or net worth requirements than those prescribed under this Rule including more stringent treatment of items in computing net capital or net worth.

(See Rule 328 for information relating to sale-and-leasebacks, factoring, financing and similar arrangements, including fixed asset loan agreements, other deductible asset loan agreements, and collateral bank loans for the purpose of determining "ready market" for securities.)