

# Interpretation Memo

Member Firm Regulation

**NYSE**

New York  
Stock Exchange, Inc.

55 Water Street  
New York, NY 10041

Number 86-3  
March 21, 1986

PLEASE ROUTE TO CHIEF FINANCIAL AND OPERATIONS  
OFFICER/PARTNER AND COMPLIANCE DIRECTORS

To: Members, Member Organizations and Handbook  
Subscribers

Subject: Potential Violation of Rule 15c3-3 in Using  
"Fluid Seg" or "Liquid Seg" Systems

In a recent letter to the New York Stock Exchange, Inc., the SEC called attention to possible violations of Rule 15c3-3 arising in segregation systems designed to secure availability of a maximum number of securities needed for delivery. Such systems will reselect excess margin securities designated for possession or control on a basis of delivery needs. In this process the system could create or increase a deficit by releasing a security which is already in possession or control and designating, in its place, a security which is not available.

A copy of the letter from the SEC is attached and should be retained with this Memo.

An interpretation Rule 15c3-3(b)/041 on the subject has been added to the accompanying Page 1021-2 which should be substituted for the present Page 1021-2 in the Interpretation Handbook.

Member organizations must carefully consider the effect of this interpretation and promptly consult with their coordinator if they have any questions.



DIVISION OF  
MARKET REGULATION

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

February 28, 1986

Mr. Edward A. Kwalwasser  
Senior Vice President  
Member Firm Regulation  
New York Stock Exchange, Inc.  
55 Water Street  
New York, N.Y.

Dear Mr. Kwalwasser:

It has come to the attention of the Division of Market Regulation that several New York Stock Exchange ("NYSE") member firms utilize so-called "Fluid Seg" or "Liquid Seg" systems for the possession or control requirements prescribed by paragraph (b) of Rule 15c3-3 under the Securities Exchange Act of 1934 (17 CFR §240.15c3-3), which may result in violations of those requirements.

These seg systems are designed to insure that a maximum number of deliveries of securities required to be made by the broker-dealer are in fact made. The system decides which securities in a particular margin account to segregate. This determination is based upon two separate processing passes. Initially, securities in customers accounts are segregated in the traditional manner. During the second pass, revisions are made to the initial release determination which is based upon the priority the system assigns to a particular security. The priorities are generally designed to create excess in the securities for which there are delivery needs.

In making such substitutions, the system may not consider the offsetting lock up requirement on the other securities in a customer's account. Hence, these procedures may result in the possible creation of deficits or the increase of deficits in the quantity of securities in other securities positions of a class and issuer required to be in possession or control. In addition, we understand that these member firms do not recall securities

Mr. Kwalwasser  
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loaned until the business day following the date of determination. This allows the system to re-cycle and results in the elimination of a substantial percentage of the deficits appearing on the prior business day. Thus, the system, by shifting the deficit from one security position to another, may permit a broker-dealer to defer indefinitely its obligations prescribed by Rule 15c3-3 to reduce all customer fully paid for and excess margin securities to its possession or control.

Rule 15c3-3 requires a broker or dealer to obtain promptly and thereafter to maintain the physical possession or control of all fully-paid and excess margin securities carried by the broker or dealer for the account of customers.

It is the view of the Division that if in using the Liquid or Fluid seg system as described above, a broker-dealer creates or increases a deficit in a particular security, the broker-dealer is violating the possession or control requirements of Rule 15c3-3.

Sincerely,



Michael A. Macchiaroli  
Assistant Director