

HOLLAND & HOLLAND

208 South LaSalle Street

Chicago, IL 60604

TELEPHONE(312) 621-9500

April 19, 1983

Mr. Julio Mojica

Securities and Exchange Commission

Department of Market Regulations

450 Fifth Street, N.W. - Stop 5-1

Washington, D.C. 20549

Re: Howe, Barnes & Johnson

Federal Funds Question

Dear Mr. Mojica:

In keeping with your request during our telephone conversation today, I am enclosing herewith copies of correspondence with the Staff of the Commission dated December 23, 1981 requesting an interpretive opinion relating to Rule 15(c)3 of the Securities Exchange Act of 1934.

Supplementing that letter is our letter of March 12, 1982 to Mr. Steven Molinari of the Division of Market Regulations covering our client's letter to us of March 10, 1982 explaining questions raised by the Staff concerning federal funds.

Supplementing those letters is a copy of confirmation from the Continental Bank to Howe, Barnes & Johnson covering the loan of federal funds by Howe, Barnes & Johnson to the Continental Bank.

Finally, we are enclosing a letter dated April 14, 1983 to Mr. George Shelton of our client from Mr. Blaise Bozzelli, Surveillance Director of the New York Stock Exchange. Mr. Bozzelli unilaterally directs Howe, Barnes & Johnson to immediately cease using federal funds of its 15(c)3-3 account. Mr. Bozzelli despite the fact that

he is on notice that Howe, Barnes & Johnson has made a request for an interpretive opinion from the S.E.C.

In our view, it appears as though Mr. Bozzelli has given himself the authority of the Commission Staff to interpret S.E.C. rules. As an entity which is registered with the Commission as a broker/dealer and also a member of the Exchange and regulated by it, you can understand the position in which this places Howe, Barnes & Johnson. Since the original request for an interpretive letter was made in December, 1981 and in light of the unilateral action taken by the New York Stock Exchange on April 14, I would respectfully request a response to our letter to Mr. Kibler at your earliest convenience.

Yours very truly,

J. William Holland

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208 South LaSalle Street

Chicago 60604

TELEPHONE(312) 621-9500

December 23, 1981

Nelson S. Kibler, Esq.

Assistant Director, Compliance and Financial Responsibility

Securities and Exchange Commission

500 North Capitol Street

Washington, D.C. 20549

Dear Mr. Kibler:

We are writing you in our capacity as counsel for Howe, Barnes & Johnson, Inc. with a request for a staff interpretive opinion relating to §15c3-3 of the '34 S.E.C. Act.

Howe, Barnes & Johnson, Inc. (hereinafter, referred to as "HB&J") is a Delaware corporation incorporated November 8, 1967 and has been, through predecessors, continuously registered as a broker/dealer with the S.E.C. since 1934.

In fulfillment of its responsibilities under Rule 15c3-3, HB&J maintains a special reserve bank account for the exclusive benefit of customers, pursuant to Rule 15c3-3(c)(1) at the Continental Illinois National Bank and Trust Company of Chicago and avails itself of that bank's offer to purchase federal funds from the account through the agency of the Federal Reserve Bank of Chicago. These amounts are carried in a federal fund sub-account for the exclusive benefit of customers.

During its regular examination of the financial statements of HB&J, its independent certified public accountants, Doherty, Zable & Company, have raised a question in connection with the aforementioned practice concerning whether the sale of federal funds to the Continental Bank, upon which a rate of return is received by our client, which is passed on to its customers, is in compliance with the terms of Rule 15c3-3.

Following conferences with the staff of Doherty, Zable & Company, it was suggested that a request for an interpretive opinion be made to your office. It is our opinion, based upon a review of the Rule, that the practice is permitted under Rule 15c3-3.

In reviewing the Rule, we note that the following terms are defined: customer, securities carried for the account of a customer, margin securities, excess margin securities, qualified security, bank, free credit balances, other credit balances and funds carried for the account of any customer Rule 15c3-3(d)(4)(e)(1) states in pertinent part that a broker or dealer shall maintain with a bank or banks at all times when deposits are required a "Special Reserve Bank Account For The Exclusive Benefit of Customers" and that it shall be separate from any other bank accounts of the broker or dealer. Further, such broker or dealer shall, at all times maintain in such reserve bank account through deposits therein, cash and/or qualified securities in amounts computed in accordance with the formula attached. The term "qualified security" in Rule 15c3-3(a)(6) means "a security issued by the United States or a security in respect of which the principal and interest are guaranteed by the United States".

In our view, federal funds are cash or the equivalent of cash and as such, the question of whether the federal funds are qualified securities need never be reached under the Rule. Although cash is issued by the United States, it is not, in our view, construed as a security. It should also be noted that despite the extensive definitional section in Rule 15c3-3(a), the term cash is not defined. We further believe that our client's position in respect of this matter is supported by the fact that an examination of our client was conducted by the Chicago Regional Office of the Securities and Exchange Commission Staff in August of 1981. The 15c3-3 account was reviewed and no deficiencies were issued by the examiner with respect to the practice of selling federal funds to the depository bank.

We would appreciate your interpretive opinion on the question.

Yours very truly,

J. William Holland

HOLLAND & HOLLAND

208 South LaSalle Street

Chicago 60604

TELEPHONE(312) 621-9500

March 12, 1982

Mr. Steven Molinari

Division of Market Regulation

Securities and Exchange Commission

500 North Capitol Street

Washington, D.C. 20549

Re: Howe, Barnes & Johnson

Federal Funds Question

Dear Mr. Molinari:

In keeping with our telephone conversation today, I am enclosing a letter to us from our client, Howe, Barnes & Johnson, Inc., explaining the analogies between federal funds and demand certificates of deposit. I understand that the Staff has interpreted demand certificates of deposit to be permitted application of funds for special reserve bank accounts for the exclusive benefit of customers.

Should you require any additional information to assist you in reaching your decision, please feel free to write or call the undersigned.

Sincerely,

J. William Holland

Howe, Barnes, & Johnson, Inc.

135 South LaSalle Street

Chicago, Illinois 60603

TELEPHONE(312) 630-2900

Holland & Holland

208 South LaSalle

Chicago, Illinois 60604

Gentlemen:

At your request we have conferred with senior officers of two major national banks concerning the nature of Federal Funds ("Fed Funds") and On Demand Certificates of Deposit ("CD's"). We determined the following.

Both Fed Funds and CD's are current obligations of the banking institution. Fed Funds are payable on demand each day. CD's are payable on demand after an Initial period required by Regulation Q of the Federal Reserve System. This initial period can be as short as 14 days although 30, 60 or 90 days are more common. Therefore, Fed Funds are more liquid than CD's while being of equal quality with them.

In terms of quality or safety, Fed Funds are also comparable to demand deposits in a checking account. Both depend on the financial condition of the bank. (FDIC coverage is insignificant in the case of multi-million dollar corporate deposits.) In this case the Institution involved is the Continental Illinois National Bank & Trust Company. It is not only the 7th largest bank in the United States but also one of the best managed and most profitable.

In terms of liquidity also, Fed Funds are comparable to demand deposits in a checking account. Fed Funds cannot be withdrawn on the same day they are committed since the commitment is for overnight; they can, however, be withdrawn at 9:00 AM the next morning. Similarly, demand deposits frequently cannot be withdrawn from a checking account until the next day because they must meet the bank's "collected funds" requirements.

In the case at hand, overnight Fed Funds are committed to the Continental Bank from our "Special Reserve Bank Account for the Exclusive Benefit of Customers." The bank shows a credit for that account on their Fed Funds ledger until the funds are re-credited to the "Special Reserve" account. Each day the bank also credits the Special Reserve account for Interest earned on the Fed Funds and substantially all of that Interest is passed on to our customers. If this cash were not held in the form of Fed Funds, our customers would be deprived of receiving the best daily return on funds they temporarily hold in their brokerage accounts pending reinvestment.

In summary, Fed Funds are "cash" and are accounted for as such by both the bank and ourselves.

Very truly yours,

George H. Shelton,

Executive Vice President

N.Y. STOCK EXCHANGE

55 WATER ST.

NEW YORK, N.Y.

TELEPHONE(212) 623-2213

Mr. George H. Shelton

Howe, Barnes & Johnson, Inc.

135 South LaSalle Street

Ste. 2040

Chicago, Illinois 60603

Dear Mr. Shelton:

This is to confirm the substance of our telephone conversation of this morning regarding the firm's practice of using federal funds to satisfy the reserve requirements of SEC Rule 15c3-3.

Notwithstanding the firm's open request for a written interpretation from the SEC, and until such is received to the contrary, the firm is hereby directed to immediately cease using federal funds to meet its reserve requirements pursuant to SEC Rule 15c3-3.

Of course, should you have any further questions, please do not hesitate to contact me.

Very truly yours,

cc: John J. Senkewich -NYSE

Virginia Mitchell -NYSE

Virgil Huggins -NYSE

Michael Macchiaroli -SEC

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Finally, we are enclosing a letter dated April 14, 1983 to Mr. George Shelton of our client from Mr. Blaise Bozzelli, Surveillance Director of the New York Stock Exchange. Mr. Bozzelli unilaterally directs Howe, Barnes & Johnson to immediately cease using federal funds in the context of its 15(c)3-3 account. Mr. Bozzelli takes this action despite the fact that he is on notice that Howe, Barnes & Johnson has made a request for an Interpretive opinion from the S.E.C.

In our view, it appears as though Mr. Bozzelli has given himself the authority of the Commission Staff to interpret S.E.C. rules. As an entity which is registered with the Commission as a broker/dealer and also a member of the Exchange and regulated



by it, you can understand the position in which this places Howe, Barnes & Johnson. Since the original request for an interpretive letter was made in December, 1981 and in light of the unilateral action taken by the New York Stock Exchange on April 14, I would respectfully request a response to our letter to Mr. Kibler at your earliest convenience.

Yours very truly,

J. William Holland

August 20, 1984

J. William Holland, Esq.

Holland & Holland

206 South LaSalle Street

Chicago, Illinois 60604

Dear Mr. Holland:

This is in response to your letter of April 19, 1983, on behalf of Howe, Barnes & Johnson ("HBJ"), in which you request an interpretative opinion regarding the use of Federal funds to satisfy the reserve requirements provided by Rule 15c3-3 under the Securities Exchange Act of 1934 (17 CFR §240.15c3-3).

We understand the pertinent facts to be as follows: HBJ is a registered broker-dealer and a member of the New York Stock Exchange ("NYSE"). In fulfillment of its responsibilities prescribed by Rule 15c3-3, HBJ maintains a Special Reserve Bank Account For the Exclusive Benefit of HBJ's Customers, ("The Special Reserve Account") at the Continental Illinois National Bank and Trust Company of Chicago ("Continental Bank"). HBJ avails itself of Continental Bank's offer to purchase Federal funds from HBJ's account through the agency of the Federal Reserve Bank of Chicago. These accounts are carried in a Federal fund sub-account for the exclusive benefit of HBJ's customers.

In the instant case, overnight Federal funds are committed to Continental bank from HBJ's Special Reserve account. Continental Bank shows a credit for the

account on its Federal funds ledger until the funds are re-credited to the Special Reserve Account. Each day the bank also credits the Special Reserve Account for interest earned on the use of the Federal funds. Substantially all of the interest earned is passed on to HBJ's customers.

Federal funds have been defined as short term loans of immediately available funds ( i.e., funds that can be transferred or withdrawn during one business day). Furthermore, Federal funds are exempt from the bank's reserve requirements and, as in this case, the vast majority of Federal funds transactions are unsecured ( i.e., the lender or seller does not receive collateral to insure him against the risk of the default by the borrower or buyer).

Rule 15c3-3 requires that a broker-dealer maintain with a bank or banks at all times when deposits are required a Special Reserve Account. The rule also requires that broker-dealers maintain in such Special Reserve Accounts through deposits made therein, cash and/or qualified securities in amounts computed in accordance with the Reserve Formula. For purposes of the Rule, Federal funds (at least those which are unsecured) are not qualified securities nor bank deposits. As such, Federal funds generated by the lending of the monies in the Special Reserve Account and "deposited" in the Special Reserve Account are in essence withdrawals from the Special Reserve Account without the computation required by paragraph (g) of Rule 15c3-3. Thus, the aforementioned transactions are not in compliance with Rule 15c3-3, and HBJ should not use Federal funds (at least, those which are uncollateralized by qualified securities as defined by Rule 15c3-3) to meet its reserve requirements pursuant to Rule 15c3-3.

We trust this is responsive to your request. Should you have any questions, please contact us.

Sincerely,

Michael A. Macchiaroli

Assistant Director

cc: Mr. Blaise Bozzelli/NYSE

Mr. George Shelton/Howe, Barnes & Johnson

Mr. William Hegan/CRO

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