National Securities Clearing Corporation

55 Water Street New York, NY 10041

TELEPHONE(212) 248-0714

October 18, 1982

Dear Mr. Kibler:

Presently, participants of National Securities Clearing Corporation's ("NSCC") Stock Borrow Program, who as a result of making securities available for borrowing by NSCC find that they have created a deficit in the amount of securities of which they must have possession or control, may instruct NSCC to convert their right to receive back the securities versus payment (represented by a Long Valued Position) into a right to receive the securities back from NSCC without payment (represented by a separate Long Free Position). These Long Free Positions are carried on NSCC's books in a separate Long Free Account. The Commission, by letter dated August 3, 1981, has taken the position that because a SIPA trustee, if one were appointed due to the impairment of a participant, would not be required to pay for the securities when returned by NSCC, positions carried in the Long Free Account representing securities due the participant may be deemed within the control of said participant for the purposes of SEC Rule 15c3-3.

NSCC intends to file a proposed rule change that would enable a participant to convert an obligation to receive securities for payment (represented by a Long Valued Position) into an obligation to receive securities without payment (represented by a Long Free Position). NSCC's rule change would permit a participant with a long position or a position due for settlement on the next business day, who in anticipation of receiving securities from NSCC as a result of the allocation process instructs that securities within his possession or control be delivered on the next business day and then fails to receive the securities during the evening allocation process, to be able to convert his Long Valued Position into a Long Free Position. Similar to that which occurs In the Stock Borrow Program, these positions would be carried on NSCC's books in a Long Free Account, NSCC would charge the participant's settlement account for the value of the securities due to be received and would mark the positions to the market daily. NSCC believes the positions which would be carried in this Long Free Account are no different from the positions carried in the Long Free Account for the Stock Borrow Program. Accordingly, NSCC believes that the good control location status previously granted for positions carried in the Long Free Account for the Stock Borrow Program should also be accorded these security positions.

The rule change addresses the fact that participants generally receive at least 75% or more of the securities due from NSCC each day as a result of the normal allocation process. However, participants do not know on any given day which securities will be among the 75% allocated. Thus, if a participant has securities which are due from NSCC, at the same time owes these securities to a third party and also has securities segregated for a customer, he only has the following options: (a) he can fail to deliver to the third party until he is actually allocated the securities by NSCC; or (b) he can go outside NSCC to borrow the securities to make the delivery and then return the securities borrowed when NSCC actually allocates the securities to him. While the participant could anticipate that he would be allocated the securities that day by NSCC and stand at least a 75% chance of being correct, he could not instruct that the securities segregated for his customer be delivered out of his control account, since, if he did not receive the allocation from NSCC and was then unable to borrow the securities, he would be in violation of SEC Rule 15c3-3. To make prompt delivery to the third party, who in many cases may be dealing on a delivery versus payment basis, participants are thus encouraged to borrow the stock before the allocation process even begins. This results in participants borrowing not only the 25% which may not be allocated, but the full 100%, thus unnecessarily increasing the borrowings by three-fold. If good control location status were accorded, the rule change would enable participants to mitigate the necessity for these increased borrowings. By eliminating unnecessary stock movements, it would also increase the efficiency of the settlement system within the national system of clearance and settlement.

By permitting a Long Valued Position to be converted into a Long Free Position under these circumstances, NSCC would be able to provide the same benefits to a SIPA trustee, if one were appointed, for an impaired participant that NSCC presenUy provides under the Stock Borrow Program arrangement, (i.e., it would guarantee the return of the securities without the obligation of the trustee to pay for the securities when delivered). Additionally, prepayment of the security positions would eliminate the market risk that NSCC would otherwise be exposed to in the event that the participant becomes impaired. By eliminating the risk, NSCC limits the losses which NSCC would seek from the SIPA trustee, if one were appointed, of the impaired participant. Accordingly, such good control status would improve the position of a SIPA trustee, if one were appointed, for an impaired participant.

Based on the above, we would request your early determination, pursuant to SEC Rule 15c3-3, as to the good control location status for securities placed in the Long Free Account under these circumstances.

Very truly yours,

Robert J. Woldow

January 25, 1984

Mr. Marc L. Weinberg

Branch Chief Clearing

Agency Regulation Securities and Exchange Commission

450 Fifth Street, N.W. Washington, D.C. 20549

Re: SR-NSCC-82-25

Dear Mr. Weinberg:

Pursuant to a meeting that was held on January 17, 1983 between the Staff of the Commission and Senior Management of NSCC, NSCC hereby agrees to make the following modification to NSCC rule filing SR- NSCC-82-25:

Procedure Section VI.E.5. - Controlling Receipts from CNS 5. Fully Paid For Account (Procedure for Movements to the Long Free Account other than for the Stock Borrow Program)

The Corporation's processing day is divided into two parts. It begins with an evening cycle on the evening preceding the business day for which the work is being processed and is followed by a day cycle which ends on the business day for which the work is processed. If a Member with a Long Position and/or a position due for settlement on the next business day, in anticipation of receiving securities from the Corporation, (other than municipal securities, as that term is defined by the Securities Exchange Act of 1934, as amended), as a result of the allocation process during the evening cycle, instructs that securities within its possession or control (other than municipal securities) be delivered on the next business day and is subsequently not allocated the securities during the evening cycle, the Member may, in order to meet the "customer segregation" requirements of SEC Rule 15c3-3, instruct the Corporation, during the following day cycle by the time specified by the Corporation, to transfer the position(s) which has not been allocated to a special CNS sub-account (the "Long Free Account). At the end of such day cycle, if the securities have still not been allocated, the Corporation will debit the Member's settlement account for the value of the position in the Long Free Account The Long Free Account will be guaranteed by the Corporation and will be marked daily. All funds which the Corporation receives from debiting the Member's settlement account for the value of a position moved into the Long Free Account and all marks credited to the Long Free Account as a result of marking positions to the market daily, will be segregated by the Corporation from all other funds received by the Corporation. Any time that a Member determines that he no longer needs the position(s) in the Long Free Account for 15c3-3 purposes, he may instruct the Corporation to transfer back the position(s) to its Long Valued Account and make the appropriate adjustment to its settlement account.

This amendment to the filing requires no additional approval by NSCC's Board.

If you have any questions regarding the above, please do not hesitate to contact me.

Very truly yours,

Karen L Saperstein

Assistant General Counsel

cc: Douglas Scarff

Director Division of Market Regulation Securities and Exchange Commission

May 10, 1984

Mr. Robert J. Woldow

Senior Vice President and General Counsel

National Securities Clearing Corporation

55 Water Street New York, New York 10041

Dear Mr. Woldow:

This is in response to your letter of October 18, 1982, on behalf of the National Securities Clearing Corporation ("NSCC") requesting a no-action position regarding "control" of customers' securities, for purposes of Securities Exchange Act Rule 15c3-3 (17 CFR §240.15c3-3), as it relates to the so-called "Long Free Account."

I understand the pertinent facts to be as follows: Currently, participants of NSCC's Stock Borrow Program, who as a result of making securities available for borrowing by NSCC find that they have created a deficit in the amount of securities of which they must have possession or control, may instruct NSCC to convert their right to receive back the securities versus payment (represented by a "Long Valued Position") into a right to receive the securities back from NSCC without payment (represented by a separate "Long Free Position"). These Long Free Positions are carried on NSCC's books in a separate Long Free Account. The Division, by letter dated August 3, 1981, has said that positions carried in the Long Free Account representing securities due the participant may be deemed within the control of that participant for purposes of Rule 15c3-3; provided that the broker or dealer does not make available to NSCC additional securities of the same class and issuer to be borrowed at the same time that it is owed securities by NSCC via the Long Free Account.

NSCC has filed a proposed rule change with the Commission (NSCC-82-25) that would permit a participant with a Long Valued Position or a position due for settlement on the next business day to anticipate receiving those securities from NSCC during the evening allocation cycle. Based on the anticipated allocation, the participant will be permitted to instruct that securities be delivered outside NSCC on the next business day. If the participant does not receive the anticipated allocation and, consequently, would have a possession or control deficit, it may convert its Long Valued Position into a Long Free Position in order to meet the requirements of Rule 15c3-3. As in the Stock Borrow Program, these positions would be carried on NSCC's books In a Long Free Account, NSCC would charge the participants money settlement account for the value of the securities due to be received and would mark the positions to the market daily. NSCC believes the positions which would be carried in this Long Free Account are no different from the positions carried in the Long Free Account for the Stock Borrow Program. Accordingly, NSCC believes that the good control status previously granted for positions carried in the Long Free Account for the Stock Borrow Program should also be accorded these positions.

You state that participants generally receive at least 75% of the securities due from NSCC each day as a result of the normal allocation process. However participants do not know on any given day which securities will be among the 75% allocated. Thus, if a participant has securities which are due from NSCC, and at the same time owes these securities to a third party, and also has securities segregated for customers, it only has the following options: (a) it can fail to deliver to the third party until it is actually allocated the securities by NSCC; or (b) it can go outside NSCC to borrow the securities to make the delivery and then return the securities borrowed when NSCC actually allocates the securities to It. While the participant could anticipate that he would be allocated the securities that day by NSCC and stand at least 75% chance of being correct, he could not instruct that the securities segregated for his customers be delivered out of his control account, since, if he did not receive the allocation from NSCC and was then unable to borrow the securities, he would be in violation of Rule 15c3-3. To make prompt delivery to the third party, who in many cases may be dealing on a delivery versus payment basis, participants are encouraged to borrow the securities before the allocation process begins. This results in participants borrowing not only the 25% which may not be allocated, but the full 100%, thus unnecessarily increasing borrowings.

You further state that by permitting a Long Valued Position to be converted into a Long Free Position under these circumstances, NSCC would be able to provide the same benefits to a Securities Investor Protection Act of 1970 ("SIPA") trustee for a participant that NSCC currently provides under the Stock Borrow Program (i.e., NSCC would unconditionally guarantee the return of the securities without the trustee being obligated to pay for the securities delivered). Additionally, prepayment of the security positions and marking the positions tions to the market daily would eliminate the market risk that NSCC would otherwise be exposed to in the event that the participant fails. By eliminating such risk, NSCC limits the losses which NSCC might seek from the SIPA trustee.

By letter dated January 25, 1984, NSCC amended the proposed rule change to provide that: (1) all funds which NSCC receives from debiting a participant's money settlement account for the value of a position moved into the Long Free Account and all marks credited to the Long Free Account as a result of marking positions to the market daily will be segregated by NSCC from all other funds received by NSSCC; and (2) municipal securities will be specifically excluded from the coverage of this proposal, because of the difficulty of buying in many municipal issues.

We also understand that NSCC will place no lien on positions held in the Long Free Account and will unconditionally guarantee delivery of the securities due the participant. Money in the Long Free Account will either be held by NSCC in bank accounts or invested in United States Treasury Bills of no more than six months duration. Ali cash and treasury bills will be held In banks account for the exclusive benefit of participants in the NSCC Long Free Account and NSCC will obtain from each bank an agreement along the lines provided for in Rule 15c3-3(f). Interest earned on the segregated long free account will accrue to NSCC and will benefit all NSCC participants. Finally, we understand that the Long Free Account takes high priority in NSCC's allocation routine, following immediately after buy-ins.

Based on the above, the Division will not recommend any action to the Commission if a broker-dealer creates or increases a deficit in the quantity of securities of a particular class and issuer required to be in its possession or control under Rule 15c3-3, by delivery out, to settle a pending delivery obligation arising from an uncompleted sales transaction, of an amount not greater than the amount of securities it anticipates receiving from NSCC during NSCC's evening allocation process. The broker-dealer must adhere to the procedures set forth in proposed Rule NSCC-82-25. The deficit may not be created or increased for any reason other than that described above such as for a bank loan or a securities loan. If the anticipated delivery from NSCC is not received, the broker-dealer must instruct

NSCC to convert its long valued position into a long free position. The broker-dealer may treat the securities due from NSCC in the long free account as if in its possession or control for a period not exceeding 14 calendar days from the initial establishment of the long free account. We intend to monitor the operation of this program. Based on this monitoring, it may be appropriate to shorten or lengthen the period of time during which a broker-dealer may treat the securities due in the long free account as if in its possession or control.

In addition, any broker-dealer that takes advantage of proposed rule NSCC-82-25 must recall deficits from bank loan and stock loan within shorter time intervals than those presently allowed under Rule 15c3-3(d)(1). In the case of bank loan, broker-dealers will be expected to effect a recall within one business day instead of the two business days presently allowed. In the case of stock loan, broker-dealers will be expected to effect a recall within two business days instead of the five days presently allowed. With regard to stock loan, the Division is aware that broker-dealers will require some time to amend stock borrow agreements between participants because such agreements currently in effect refer to the five day period. Accordingly, the Division will recommend no action to the Commission if broker-dealers do not comply with the stock loan recall condition until the Division will recommend no action to the Commission if broker-dealers do not comply with the stock loan recall condition until October 1, 1984.

Finally, NSCC has agreed to provide the Division with a monthly report summarizing the use by broker- dealers of the Long Free Account, including the number of broker-dealers which have used the account during the month, the amount of money segregated by NSCC pursuant to the program at the end of the month, and the average daily amount in the Long Free Account. NSCC will also disclose in the report the name of any broker-dealer who at month end has an amount exceeding $5,000,000 in its Long Free Account and the amount in that account.

Sincerely,

Michael A. Macchiaroli

Assistant Director