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

DIVISION OF
MARKET REGULATION

August 18, 1988

Mr. Edward Kwalwasser
Senior Vice President
New York Stock Exchange, Inc.
20 Broad Street
New York, NY 10005

Mr. Thomas R. Cassella
Vice-President
National Association of
Securities Dealers, Inc.
1735 K Street, N.W.
Washington, DC 20006

Dear Messrs. Kwalwasser and Cassella:

This responds to the various questions received from registered broker-dealers, which are members of your organizations, regarding the current charges imposed by the Net Capital Rule (17 CFR §240.15c3-1), under the Securities Exchange Act of 1934, on so-called "municipal put-bonds" held in their accounts.

We understand certain issuers of municipal securities have attached to certain issues of variable or floating rate municipal securities non-severable periodic demand features which entitle the holder to put the underlying securities to the issuers at their par values at designated times.

To avoid reissuance problems with the Internal Revenue Service, the municipal securities are put to a third party who remarkets the instruments to the investing public. This third party, the issuer's remarketing agent, is also solely responsible for adjusting the interest rate on the interest reset date so that the market value of the instrument may reasonably approximate its par value. Furthermore, as an agent of the issuer, the remarketing agent has no initial obligation or commitment to purchase the issuer's securities that he has failed to remarket.

The periodic nature of the demand feature restricts the holder's right to exercise his put within a specific time period after giving the required amount of notice, which varies among different issues. As the specified interval increases, the notice requirement may also increase with thirty (30) days as the usual, maximum amount.

The right of the holder to put the security to the issuer lasts for the life of the underlying security, i.e., until maturity or redemption by the issuer prior to maturity. Thus, until the instrument becomes due and payable, the holder may receive the principal amount of the underlying security from the issuer by simply exercising his put. Moreover, the floating or variable interest rate paid on the underlying security causes the market value of the instrument to approximate its par value. As a result, the holder's market risk associated with such an instrument is reduced considerably and corresponds more closely to short-term, fixed-rate municipal securities. Such securities ordinarily receive credit ratings indicative of short-term instruments. In addition, those securities which can be converted to bear interest at a fixed rate often are assigned credit ratings as long-term instruments.

Generally, an issuer supports its ability to satisfy the holder's demand with an irrevocable letter of credit, a standby bond purchase agreement or other liquidity facility. This third-party credit support ensures the availability of sufficient funds to allow a holder to recover the principal amount of the instrument upon the exercise of the demand feature. Use of the third-party credit support would only occur if the remarketing agent fails to remarket the security that has been put to the issuer. Once a draw has occurred, a loan exists between the issuer and the bank or other purchaser with the security in the possession of the third party as collateral. Securities for which the issuer does not obtain a letter of credit, a standby bond purchase agreement or other liquidity facility are evaluated and rated on the basis of the credit-worthiness of the issuer or other party on whose behalf the securities have been issued.

With respect to the floating or variable rate municipal securities with a non-severable periodic demand feature described above, and which normally trade at par, the Division of Market Regulation will raise no question nor recommend any action if registered broker-dealers take only a one (1) percent

haircut on the aggregate principal amount of the positions found in their proprietary accounts, rather than the haircut otherwise required by subparagraph (c)(2)(vi)(B)(2) of Rule 15c3-1.

Sincerely,

Michael A. Macchiaroli

Michael A. Macchiaroli
Assistant Director