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

DIVISION OF
MARKET REGULATION

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 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

Michael A. Macchiaroli
Assistant Director