



DIVISION OF  
MARKET REGULATION

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

August 13, 1993

Dominic A. Carone  
Chairman  
Capital Committee  
Securities Industry Association  
120 Broadway  
New York, New York 10271

Re: Ready Marketability of Foreign Equity Securities

Dear Mr. Carone:

Your letter, dated October 8, 1992,<sup>1/</sup> requests on behalf of the Capital Committee of the Securities Industry Association ("SIA"), that the Division of Market Regulation ("Division") advise the SIA, on behalf of its members and similarly situated broker-dealers, that the Division will not recommend that the Commission take enforcement action if broker-dealers treat the foreign equity issues that are listed on the FT-Actuaries World Indexes (the "Indexes") as having a ready market with respect to the ready market and haircut provisions of Rule 15c3-1 of the Securities Exchange Act of 1934 (17 C.F.R. § 240.15c3-1) ("Rule").

I.

In determining a broker-dealer's net capital under the Rule, a broker-dealer is required generally to deduct from net worth as computed in accordance with generally accepted accounting principles, assets not readily convertible into cash, most unsecured receivables, and certain percentage deductions related to the securities positions that it carries. Paragraph (c)(2)(vi) of the Rule includes a 100% deduction for securities held by a broker-dealer for which there is no ready market as defined in paragraph (c)(11) of the Rule. A lesser deduction is required for securities which are deemed to have a ready market.

With respect to foreign securities, in December 1975, the Division issued an interpretive letter deeming a "ready market" to

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1/ Letter from Dominic A. Carone, Chairman, Capital Committee, Securities Industry Association, to Michael A. Macchiaroli, Assistant Director, Division of Market Regulation, dated October 22, 1992.

exist in certain circumstances.<sup>2/</sup> Specifically, as described in that letter, only foreign equity securities that were publicly issued in a principal securities market and are listed on one of the principal exchanges in the major money markets outside the United States are deemed to have ready markets and receive haircuts similar to comparable United States securities traded on United States markets. The 12 exchanges in 11 countries which the Division recognized as being "principal exchanges in the major money markets" are: Amsterdam, Brussels, Frankfurt, Johannesburg, London, Luxembourg, Montreal, Paris, Sydney, Tokyo, Toronto, and Zurich.<sup>3/</sup>

In your letter, you state that "since 1975, new foreign securities markets have been established and the volume of trading in foreign securities by U.S. broker-dealers has significantly increased," thus, causing U.S. broker-dealers to compete in a global marketplace. You argue that U.S. broker-dealers are adversely affected in this global marketplace because the interpretation of ready market contained in the 1975 letter no longer accurately assesses the liquidity of foreign equity securities. Thus, the SIA Capital Committee recommends that the Division recommend no action if broker-dealers treat the foreign equity securities listed on the FT-Actuaries World Indices as having a ready market.<sup>4/</sup>

## II.

The FT-A World Indices are jointly compiled by The Financial Times Limited, Goldman, Sachs & Co., and County NatWest/Wood Mackenzie (together, the "Consortium") in conjunction with The Institute of Actuaries and The Faculty of Actuaries. The aim of the Consortium was to create and maintain a series of high-quality equity market indices for use by the global investment community.

The Consortium reviews annually the exchanges to be included in the indices. In determining which exchanges to include the

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- 2/ Letter from Nelson S. Kibler, Assistant Director, Division of Market Regulation, to Anthony M. O'Connor, Co-Chairman, International Committee, SIA, dated December 29, 1975.
- 3/ Letter from Nelson S. Kibler, Assistant Director, Division of Market Regulation, to Anthony M. O'Connor, Co-Chairman, International Committee, Securities Industry Association, dated December 29, 1975.
- 4/ The components of the Indices will be made available to the New York Stock Exchange and the National Association of Securities Dealers on a quarterly basis for distribution to their members. Reliance may be placed on the quarterly Indices until publication of the following quarterly Indices.

Consortium looks at the following criteria: direct equity investment by non-nationals must be available; accurate and timely data must be available; no significant exchange controls should exist which would prevent the timely repatriation of capital or dividends; significant international investor interest in the local equity market must have been demonstrated; and adequate liquidity must exist.

We understand that, in determining which issues to include on the Indices the Consortium subjects the issues listed in the different markets to five investibility screens to determine the investible universe. The first screen, the Size Screen, excludes the bottom 5% of any market's capitalization. The second screen, the Total Restriction Screen, excludes any foreign security which foreign investors are barred from owning. The third screen, the Partial Restriction Screen, excludes a portion of the capitalization of an issue where the security has restrictions on foreign ownership. A fourth screen, the "Free Float" Screen, generally excludes a security where one or more identifiable holders acting in concert holds more than 75% of the outstanding issue. The fifth screen, the Liquidity Screen, excludes any security that fails to trade for more than fifteen working days within each of two successive quarters.

Once the Consortium has determined the investible universe for a given market, it selects constituent stocks in order to capture about 85% of this investible universe. The Consortium also determines the economic sectoral make-up of each market before determining the individual stocks to include. The stocks are selected so that the index reflects the economic sector distribution of the investible universe.

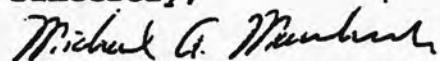
### III.

Based on the above, the Division will not recommend to the Commission that enforcement action be taken as to section 15(c)(3) of the Securities Exchange Act of 1934 and Rule 15c3-1 thereunder if broker-dealers treat foreign equity securities listed on the FT-A World Indices as having a ready market for the purposes of the Rule. These securities will be subject to the haircuts specified under paragraph (c)(2)(vi)(J). All prior staff opinions relating to the ready marketability of foreign equity securities, including those contained in the letter to Anthony O'Connor of the SIA International Committee, dated December 29, 1975, are hereby withdrawn and should not be relied upon. You also should note that this letter is not intended to validate the use of the Indexes in any other context, but that the relief provided by this no-action letter is limited specifically to the terms herein.

You should be aware that this is a staff position with respect to enforcement action only and does not purport to express any legal conclusions. This position is based solely on the foregoing

description; any factual variations may warrant a different response. This position may be withdrawn or modified if the staff determines that such action is necessary in the public interest, for the protection of investors, or otherwise, in furtherance of the purposes of the securities laws. In any event, the position stated herein will be reviewed by June 30, 1995. We expect to work with your Committee in determining the efficacy of this approach.

Sincerely,



Michael A. Macchiaroli  
Associate Director

Mr. Guillermo T. Prieto  
August 28, 1992

If you have any questions concerning these matters, please do not hesitate to contact us.

Sincerely,

*Michael A. Macchiaroli*  
Michael A. Macchiaroli  
Assistant Director