



DIVISION OF
MARKET REGULATION

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

Public Reference Copy

August 21, 1992

Douglas G. Preston, Esq.
Securities Industry Association, Inc.
120 Broadway
New York, NY 10271

Dear Mr. Preston:

This is in response to a letter to the Securities and Exchange Commission ("Commission") dated July 6, 1989 on behalf of the Securities Industry Association ("SIA"). That letter requests clarification as to the deductibility of money market instruments issued by financial institutions for purposes of calculating net capital under the Uniform Net Capital Rule, rule 15c3-1 under the Securities Exchange Act of 1934 ("Exchange Act").¹

Paragraph (c)(2)(vii) of the Uniform Net Capital Rule requires, for purposes of computing net capital, that a broker-dealer deduct 100% of the carrying value of securities or evidence of indebtedness in its proprietary accounts whenever there is no ready market for such securities or evidence of indebtedness.² Questions have been raised regarding to what extent money market instruments issued by financial institutions (including so-called "936 money market instruments" of the same kind), have a ready market.³

I. Money market instruments issued by financial institutions

As used in this letter, the term "money market instruments" will refer to borrowing by financial institutions evidenced by instruments such as bankers acceptances,⁴ certificates of deposit,⁵ bills of exchange,⁶ and bank deposit notes.⁷

¹ 17 C.F.R. § 240.15c3-1.

² 17 C.F.R. § 240.15c3-1(c)(2)(vii). See 17 C.F.R. § 240.15c3-1(c)(11)(i) (defining the term "ready market" as used in the Uniform Net Capital Rule).

³ Questions concerning "936 money market instruments" in Puerto Rico also have arisen because of the federal taxation regime applicable to income earned in that territory of the United States.

⁴ A bankers acceptance is a time draft drawn on and accepted by a bank. Bankers acceptances are the customary means of effecting payment for merchandise sold in import-export transactions and are a source of financing used extensively in international trade.

⁵ A certificate of deposit is a debt obligation issued as evidence that a specific amount of money has been deposited with a depository institution for a fixed period of time at an agreed rate of interest.

⁶ A bill of exchange or "bank bill" is an uncollateralized negotiable money market instrument that resembles a bankers acceptance. Bills of exchange are used mainly to effect short-term (continued...)

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Questions have been raised as to whether money market instruments have a "ready market;" that is, whether they can be sold in a recognized securities market in which,

there exists independent *bona fide* offers to buy and sell so that a price reasonably related to the last sales price or current *bona fide* competitive bid and offer quotations can be determined for a particular security almost instantaneously and where payment will be received in settlement of a sale at such price within a relatively short time conforming to trade custom.⁶

From the perspective of the Uniform Net Capital Rule, if positions in money market instruments are deemed to lack a ready market, broker-dealers would be required to deduct 100% of the carrying value of these positions in their proprietary accounts.⁷

The SIA asserts that money market instruments are readily acceptable as collateral for bank loans. According to the SIA letter, the liquidity of money market instruments is demonstrated by, among other things, the fact that many entities, in accordance with generally accepted accounting principles, include money market instruments under the heading "cash and cash equivalents" in their financial statements.

II. Section 936 market

As a result of the beneficial tax treatment provided by section 936 of the Internal Revenue Code ("section 936")⁸, mainland businesses operating in Puerto Rico invest qualifying income earned in Puerto Rico in local financial institutions in the form of money market instruments. To qualify for the tax credit provided to investment income by section 936, such investment income must (i) be derived from sources within a possession of the United States, including Puerto Rico, and (ii) be "attributable to the investment in such possession (for use therein) of funds derived from the active conduct of a trade or business in such possession, or from such investment."⁹ Accordingly, many of the money

⁶(...continued)

borrowing and lending. They are usually denominated in amounts greater than \$100,000 and have maturities between 90 and 180 days.

⁷ A bank deposit note, also referred to as a medium term deposit note or a certificate of deposit note, is an obligation issued by a U.S. bank or a foreign bank through its U.S. branch. In most cases, bank deposit notes are unsecured obligations that rank *pari passu* with all other unsecured and non-subordinated debt. The maturity range of these notes is generally between eighteen months and ten years.

⁸ 17 C.F.R. § 240.15c3-1(c)(11)(i).

⁹ 17 C.F.R. § 240.15c3-1(c)(2)(vii).

¹⁰ 26 U.S.C. § 936.

¹¹ 26 U.S.C. § 936(d)(2)(B).

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market instruments sold in Puerto Rico are designed to comply with the requirements of section 936, thus allowing purchasers to take advantage of the tax credit provided under section 936. As a result of this situation, the market for these money market instruments, when sold outside Puerto Rico, will be substantially different, reflecting the fact that they no longer convey the same tax advantages.

The SIA claims that the 936 market is a liquid securities market within Puerto Rico with total investments of approximately \$13 billion. This market, moreover, involves many foreign and domestic financial institutions who often guarantee the obligations sold to lenders by issuing unconditional letters of credit that serve to back the payment of principal and interest on such underlying obligations.

III. Conclusion

Based on the above facts, and with regard to the issues set forth in this letter, the Division will not recommend to the Commission that enforcement action be taken for violations of section 15(c)(3) of the Exchange Act¹² and rule 15c3-1(c)(2)(vii)¹³ thereunder if broker-dealers do not deduct the full market value of the instruments described below under the circumstances described below:¹⁴

A. MONEY MARKET INSTRUMENTS

1. The following proprietary positions may be deemed to have a ready market under subparagraph (c)(2)(vii) of the Uniform Net Capital Rule and not subject to a deduction of 100% of its carrying value, if one or more of the conditions set forth in paragraphs (A), (B) or (C), below are met.
 - (a) negotiable certificates of deposit and bank deposit notes,
 - (i) that are not issued by a parent or an affiliated company of the broker-dealer, and
 - (ii) where the funds are deposited and payable in a major money market.¹⁵

¹² 15 U.S.C. § 78o(c)(3).

¹³ 17 C.F.R. § 240.15c3-1(c)(2)(vii).

¹⁴ The purpose of this letter is to provide a safe harbor regarding the classification of certain proprietary positions in money market instruments under subparagraph (c)(2)(vi)(E) of the Uniform Net Capital Rule. A broker-dealer may elect to include other proprietary positions in money market instruments if it can demonstrate that there exists a ready market for such positions.

¹⁵ For purposes of this letter only, the major money markets include:

Australia

Austria

Belgium

Canada

(continued...)

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- (b) negotiable bankers acceptances and bills of exchange that,
 - (i) are not issued or accepted by a parent or an affiliated company of the broker-dealer, and
 - (ii) are issued or accepted by a bank when the obligation is booked and payable in a major money market.

Conditions:

- (A) The certificate of deposit or bank deposit note is issued or unconditionally guaranteed as to principal and interest, or the bankers acceptance or bill of exchange is issued or accepted as to principal and interest by:
 - (1) a bank as defined in section 3(a)(6) of the Exchange Act¹⁶ or a building and loan or savings and loan institution, and such bank, building and loan or savings and loan institution is:
 - (a) subject to supervision by a federal banking authority, and
 - (b) rated investment grade by at least two of the nationally recognized statistical rating organizations ("NRSROs").
 - (2) a bank as defined in section 3(a)(6) of the Exchange Act that:
 - (a) is not rated,
 - (b) has shareholders' equity of at least \$400 million, and
 - (c) is subject to supervision by a federal banking authority.
 - (3) a building and loan or savings and loan institution that:
 - (a) is not rated,

¹⁵(...continued)

Denmark	Finland	France	Germany
Greece	Hong Kong	Ireland	Italy
Japan	Luxembourg	Netherlands	New Zealand
Norway	Portugal	Singapore	Spain
Sweden	Switzerland	United States	United Kingdom

- (b) that is subject to supervision by a federal banking authority, and
- (c) has shareholders' equity of at least \$500 million.

(B) The certificate of deposit, bank deposit note, bankers acceptance or bill of exchange is rated investment grade by at least two NRSROs and is issued or accepted as to principal and interest by a foreign commercial bank,

- (1) that has shareholders' equity of at least US\$1 billion, and
- (2) whose capital is subject to supervision by an authority of a sovereign national government where a major money market is located.

(C) The certificate of deposit, bank deposit note, bankers acceptance or bill of exchange is issued or accepted as to principal and interest by a foreign commercial bank,

- (1) that has shareholders' equity of at least US\$1.5 billion,
- (2) whose capital is subject to supervision by an authority of a sovereign national government where a major money market is located, and
- (3) that is not rated.

2. If a broker-dealer holds a combined position consisting of negotiable or non-negotiable certificates of deposit, bank deposit notes, bankers acceptances or bills of exchange issued or unconditionally guaranteed as to principal and interest, or accepted as to principal and interest by (i) a single bank as defined in section 3(a)(6) of the Exchange Act, or (ii) a single building and loan or savings and loan institution, or (iii) a single foreign commercial bank, which combined position is in the proprietary or other account of a broker-dealer for more than five business days, there shall be a deduction from net worth equal to 100% of the carrying value of that position exceeding 30% of the broker-dealer's net capital before the application of the adjustment set forth in subparagraph (c)(2)(vi) or (f)(3) and Appendices A and B of the Uniform Net Capital Rule.¹⁷

¹⁷

17 C.F.R. §§ 240.15c3-1(c)(2)(vi) or .15c3-1(f)(3) and 240.15c3-1a & 240.15c3-1b.

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B. SECTION 936 MARKET

Negotiable certificates of deposit and bank deposit notes ("obligations") which are sold in Puerto Rico for the section 936 market, may be deemed to have a ready market under subparagraph (c)(2)(vi) of the Uniform Net Capital Rule and not subject to a deduction of 100% of its carrying value, provided that the following conditions are met:

1. the obligations are not issued by a parent or an affiliated company of the broker-dealer, and
2. the purchase of the obligations by a corporation that is allowed a tax credit pursuant to section 936 or that is an "eligible institution under Regulation Number 3582 of the Commissioner of Financial Institutions of the Commonwealth of Puerto Rico ("Reg. 3582"), constitutes, either
 - (a) an investment under section 936(d)(2) of the Internal Revenue Code for the purpose of deriving "Qualified Possession Source Investment Income," or
 - (b) an investment in an "eligible activity" under section 6.2.4 of Reg. 3582, and
 - (c) in either instance, the funds securing such obligations are deposited and payable in the Commonwealth of Puerto Rico, provided that one or more of the conditions set forth in paragraphs (A), (B) or (C) below are met.

Conditions:

- (A) The obligations are issued by, or backed, absolutely and without condition (as to principal and interest), by an irrevocable letter of credit issued by
 - (1) a bank as defined in section 3(a)(6) of the Exchange Act or a building and loan or savings and loan institution which is:
 - (a) subject to supervision by a federal banking authority, and
 - (b) rated in one of the two highest grades by at least two NRSROs.
 - (2) a bank as defined in section 3(a)(6) of the Exchange Act that:
 - (a) is not rated,
 - (b) has stockholders' equity of at least \$400 million, and

- (c) is subject to supervision by a federal banking authority.
- (3) a building and loan or savings and loan institution that:
 - (a) is not rated,
 - (b) has stockholders' equity of at least \$500 million, and
 - (c) is subject to supervision by a federal banking authority.
- (B) The obligations are backed absolutely and without condition (as to principal and interest) by an irrevocable letter of credit issued by a foreign commercial bank rated in one of the two highest grades by at least two NRSROs,
 - (1) that has shareholders' equity of at least US\$1 billion, and
 - (2) whose capital is subject to supervision by an authority of a sovereign national government where a major money market is located.
- (C) The obligations are backed (as to principal and interest) by an irrevocable letter of credit issued by a Federal Home Loan Bank or an agency of the Federal Government of the U.S.

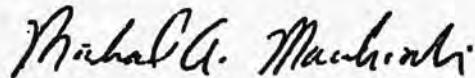
- C. Non-negotiable certificates of deposit that would otherwise qualify for treatment under one or more of the provisions set forth in either sections A. or B. above, for which the only restriction relative to early withdrawal at any time prior to maturity is the forfeiture of interest may be included under subparagraph (c)(2)(vi)(E) of the Uniform Net Capital Rule¹⁸ if the broker-dealer takes an additional deduction for the amount of interest subject to forfeiture.
- D. With regard to money market instruments that are deemed to have a ready market under section A. and B. above: if either of the ratings required to qualify a money market instrument as having a ready market is reduced below the two highest ratings categories, the broker-dealer holding such money market instrument will deduct from net worth, when computing net capital, 15% of the carrying value of the money market instruments. At the end of 30 days subsequent to the date when any of the two ratings is reduced below the two highest categories, if the broker-dealer continues to hold the position it must prove otherwise that the money market instruments have a ready market in order to include such position under subparagraph (c)(2)(vi)(E) of the Uniform Net Capital Rule.

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This is a staff position concerning enforcement action and it does not represent any legal conclusions. This position is based solely on the foregoing description and factual variations might require 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.

If you have any questions regarding these matters, please do not hesitate to contact Julius R. Leiman-Carbia at (202) 272-2824.

Sincerely,



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Assistant Director

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15c3-1(c)(2)(iii)

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CC: - 15c3-1(c)(11)

Washington Service Bureau, Inc.
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July 6, 1989

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Act Section Rule
1934 15(c)(3) 15c3-1

By Federal Express

Mr. Michael A. Macchiaroli
Assistant Director
Division of Market Regulation
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, DC 20549

Dear Mr. Macchiaroli:

This letter is submitted on behalf of the Capital Committee of the Securities Industry Association ("SIA").^{1/} SIA is seeking a no action letter with respect to the term "ready market", as defined in paragraph (c)(11) of Rule 15c3-1 (the "Net Capital Rule") of the Securities Exchange Act of 1934, and its application to money market instruments for purposes of determining capital charges under subparagraph (c)(2)(vii) of the Net Capital Rule. Subparagraph (c)(2)(vii) states that "a broker-dealer shall deduct from net capital 100 percent of the carrying value of securities or evidences of indebtedness in the proprietary or other accounts of the broker-dealer for which there is no ready market, as defined in subparagraph (c)(11)" of the Net Capital Rule. Subsection (c)(11)(i) states that "the term 'Ready Market' shall include a recognized

1/ The Securities Industry Association is the trade association representing over 575 securities firms headquartered throughout the United States and Canada. Its members include securities organizations of virtually all types--investment banks, brokers, dealers and mutual fund companies, as well as other firms functioning on the floors of the exchanges. SIA members are active in all exchange markets, in the over-the-counter market and in all phases of corporate and public finance. Collectively, they provide investors with a full spectrum of securities and investment services and account for approximately 90% of the securities business being done in North America.

established securities market in which there exists independent bona fide offers to buy and sell so that a price reasonably related to the last sales price or current bona fide competitive bid and offer quotations can be determined for a particular security almost instantaneously and where payment will be received in settlement of a sale at such price within a relatively short time conforming to trade custom."

Although money market instruments are not traded on a formally "recognized established securities market", we believe, as explained in our discussion below, that the markets on which they trade possess the characteristics, i.e: marketability and liquidity, that the criteria set forth in subparagraph (c)(11)(i) seek to establish. In view of this, we have drafted a proposed interpretation to subparagraph (c)(11) which, we believe recognizes the marketability and liquidity of money market instruments and, we are requesting that you advise us that you will not recommend to the Commission that enforcement action be taken if a broker-dealer applies the proposed interpretation for purposes of determining whether a ready market exists for commercial paper, bankers acceptances and deposit and debt obligations issued by depository institutions. Our analysis and proposed interpretation follow.

DISCUSSION

The vast majority of money market instruments, including commercial paper, bankers acceptances and deposit and debt obligations issued by depository institutions, range in various maturities up to nine months and are negotiable, investment grade and highly liquid. In fact, they are so liquid that for presentation in financial statements prepared in accordance with generally accepted accounting principles many entities often include these instruments in the caption "Cash and Cash Equivalents." In addition, there is a very active market in one to five year certificates of deposit.

The fact that there is no stream of bids and offers for these types of instruments by specific issuer, specific interest rate and maturity certainly would indicate that these instruments are as marketable as cash. The volume in these investments is in the billions. Although these instruments are often held to maturity, if the need to liquidate arises, it can be accomplished in a very liquid secondary market by a telephone call to any major bank dealer or major broker-dealer. We believe it is clear that money market instruments are readily marketable and liquid. Additionally, money market instruments are readily acceptable as collateral for bank loans.

COMMERCIAL PAPER

Commercial Paper outstanding on May 31, 1989 was approximately \$501 billion (see Exhibit 1) with approximately \$29 billion (see Exhibit 2) transacted daily. The Federal Reserve Bank of New York, (the "FED") publishes a daily quote for 1, 2, and 3 month A1/P1 paper.

For the reasons discussed below, 3(a)(2), 3(a)(3) and 4(2) paper are virtually identical and should be treated equally under the Net Capital Rule. For example, in regard to the traditional commercial paper characteristics, 4(2) paper has maturities of less than 270 days, is prime quality, is discountable at Federal Reserve Banks and is not purchased by the general public. The only reason that an issuer would use the 4(2) exemption instead of the 3(a)(3) exemption is because the proceeds of the issue are not used for "current transactions", as required by the Section 3(a)(3) exemption.

Generally, investors distinguish between commercial paper issuers on the basis of the characteristics of the issuer *i.e.*: credit of the issuer, maturities offered and rate and not the particular exemption under which the paper is issued. For the most part, purchasers of commercial paper are indifferent as to whether the commercial paper is 3(a)(2), 3(a)(3) paper or 4(2) paper because in those instances where an issuer has a combination of 3(a)(2), 3(a)(3) and 4(2) paper programs, the interest rates, maturity dates and the secondary market bids and asks are identical for each type of paper. The fact that the market imposes no discount on the 4(2) paper is compelling evidence that the credit and market risks are identical for each type of paper.

Additionally, the rating agencies treat 3(a)(2), 3(a)(3) paper and 4(2) paper identically. In those instances where an issuer has a combination of 3(a)(2), 3(a)(3) and a 4(2) program, each type of paper always receive the same rating from Standard & Poor's. Moody's rates issuers, not issues and in so doing does not distinguish in the event that some of a particular issuer's paper is 4(2) paper.

Additionally, the vast majority of customers who buy 3(a)(2) and 3(a)(3) paper also buy 4(2) paper. According to our informal poll of the active money market investors that purchase 3(a)(3) paper, approximately 60-70% also buy 4(2) paper. Furthermore, the 4(2) investors comprise the same investor categories as the 3(a)(3) purchasers; all are large and sophisticated institutions who will often purchase commercial paper in blocks averaging \$3 million. Examples of these investors are mutual funds, insurance companies and pension funds. The 30-40% who do not purchase 4(2) paper are

fairly evenly distributed in all investor categories. While the remaining 30-40% have diverse reasons for not purchasing 4(2) paper, the reasons often relate to the entities' original authority to make certain investments. For example, many funds cannot purchase 4(2) paper because such paper did not exist in meaningful quantities at the time the fund was formed and the prospectus for the fund has not been amended to authorize such purchases.

The liquidity of 4(2) paper is on a par with the liquidity of 3(a)(2) and 3(a)(3) paper as evidenced by the depth and breadth of potential investors. The net capital requirement that a security must have the capability of being publicly sold must be analyzed in the context of the commercial paper market and the extremely short term maturities involved. The same "public" that buys 3(a)(2), 3(a)(3) paper buys 4(2) paper--it is a sophisticated and wealthy "public" that does not necessarily distinguish between the type of commercial paper for sale. In view of the fact that it is the same universe of investors, it is merely semantics, and of no potential effect (except for the issuers' use of the proceeds), for an issuer to sell commercial paper via the 3(a)(2), 3(a)(3) or 4(2) exemptions. The investors are the same, the interest rates are the same, and the ratings are the same--the only thing that changes is the documentation required to comply with the Securities Act of 1933. Even the Federal Reserve Banks treat 3(a)(2), 3(a)(3) and 4(2) paper identically. Each type of paper is fully discountable at a Federal Reserve Bank, meaning that a broker-dealer can obtain 100% collateral value on such paper. Certainly such a source of cash should allay any illiquidity concerns.

BANKERS ACCEPTANCES

Based on Fed data published in April 1989, the acceptance market at December 1988 had approximately \$67 billion outstanding and currently trades approximately \$2.2 billion daily (see Exhibit 2). There are two brokers who have screens and act between the approximately 40 recognized dealers. Effectively, the market only goes out to six months, thereby providing excellent liquidity in these instruments. Bankers Acceptances are collateralized instruments and occasionally the Fed loans against them and sometimes buys them outright.

CERTIFICATES OF DEPOSIT

The domestic CD market had approximately \$45 billion outstanding at June 30, 1988 with current average daily volume of approximately \$1.3 billion for domestic CDs and approximately \$1.3 billion for foreign CDs (see Exhibit 2). The Fed publishes a daily rate for 1, 3, and 6 month CDs of top

tiered domestic banks. These Fed rates act as a benchmark rate with which other rates can be compared. Additionally, there are two domestic brokers who facilitate trades between the domestic money market dealers. The brokers' screens and dealer market making along with trades with retail customers provide complete price information.

In the Euro CD market (\$180 billion outstanding at March 1988) there are approximately eight brokers in New York and another eight in London. On the average, New York brokers deal with approximately 100 clients, dealers and banks, and the London brokers have approximately 200 clients each. Needless to say, this provides a great deal of price information as well as marketability.

BILLS OF EXCHANGE
"BANK BILLS"

Bank bills are uncollateralized negotiable market instruments which resemble bankers acceptances. They are used mainly to effect short-term borrowing and lending and are usually denominated in amounts over \$100,000 with maturities between 90-180 days. The level of bills outstanding accepted/endorsed by trading banks was \$10 billion at mid 1988. Additionally, futures contracts in bank bills are traded on the Sydney Exchange.

BANK DEPOSIT NOTES

Deposit notes, also referred to as Medium Term Deposit Notes or CD Notes, are obligations issued by domestic banks and foreign banks via their U.S. branches. The maturity ranges of these deposit note programs are generally between 18 months to 10 years. Over \$20 billion of deposit notes were outstanding as of June 30, 1988. In most cases, they are unsecured obligations ranking pari passu with all other unsecured and unsubordinated debt.

For the reasons set forth above, we believe that the following proposed interpretation of paragraph (c)(11) of the Net Capital Rule adequately addresses the Commission's concerns regarding money market instruments while acknowledging the practical realities of the market place.

PROPOSED INTERPRETATION FOR
DEFINITION OF READY MARKET

A ready market shall be deemed to exist for the following negotiable money market instruments or similar types of

instruments (whether fixed or variable rates) under the indicated conditions which constitute a recognized established securities market for purposes of subparagraph (c)(11) of Rule 15c3-1. (Note, however, that certain of these instruments may not be securities):

- 1) Commercial Paper - Issued pursuant to Securities Act of 1933 sections 3(a)(2), 3(a)(3) and 4(2)
 - (a) Rated investment grade by at least two nationally recognized statistical rating organizations.
 - (b) If not rated by a nationally recognized statistical rating service, but the issuer has outstanding non-convertible debt which is rated in one of the four highest rating categories by at least two of the nationally recognized statistical rating organizations.
 - (c) If guaranteed by a company that has short term commercial paper rated investment grade by two nationally recognized statistical rating organizations or has non-convertible debt which is rated in one of the four highest rating categories by at least two of the nationally recognized statistical rating organizations.
 - (d) If not rated, but is collateralized by an irrevocable letter of credit issued by a bank as defined in items (e), 4 and 5 below.
 - (e) If criteria not met as indicated in (a), (b), (c) or (d) above, but is acceptable collateral for a loan with an unaffiliated entity meeting one of the following requirements:
 - 1) A member of a United States national securities or commodities exchange.
 - 2) A member of a United States national securities or commodities association.
 - 3) A member of a foreign exchange or regulated securities broker-dealer located in Australia, Austria, Belgium, Canada, Denmark, Federal Republic of Germany, Finland, France, Hong Kong, Italy, Japan, Luxembourg, Malaysia, Netherlands, New Zealand, Norway, Portugal, Singapore, South Africa, Spain, Sweden, Switzerland and the United Kingdom.

4) A domestic bank as defined in Section 3(a)(6) of the Securities Exchange Act of 1934 or any U.S. depository institution with net assets of \$100 million.

5) A foreign bank with net assets of \$100 million which is located in Australia, Canada and Japan or in a country which is a member of the European Economic Community.

The commercial paper in (a), (b), (c), (d) and (e) above would be subject to the haircuts currently provided by Rule 15c3-1(c)(2)(vi)(e), plus undue concentration, if appropriate.

Other commercial paper would be deemed readily marketable subject to a 15% haircut, plus undue concentration, if appropriate, if held in inventory for no longer than five business days. All other commercial paper would be 100% haircut.

2) Bankers Acceptances, Deposit And Debt Obligations Issued By Depository Institutions*

- (a) Rated investment grade by two nationally recognized statistical rating organizations.
- (b) If not rated, but the issuing depository institution has other non-convertible debt rated in one of the four highest rating categories by at least two of the nationally recognized statistical rating organizations.
- (c) United States depository institutions with net assets of \$100 million and major money market financial institutions with net assets in excess of \$100 million which are subject to supervision by an authority of a sovereign national government included in 1(e)3 and 5 above.
- (d) Non-negotiable certificates of deposit subject to immediate withdrawal at any time if issued by an entity that qualifies in (a) through (c) above.
- (e) If criteria not met as indicated in (a), (b), (c) or (d) above, but is acceptable collateral for a bank loan with an unaffiliated entity.

Bankers acceptances, deposit and debt obligations issued by depository institutions, meeting the criteria in (a), (b), (c), (d) and (e) above would be subject to the haircuts currently prescribed by Rule 15c3-1(c)(2)(vi)(e), including undue concentration, if appropriate. In addition, additional deduction should be made for any early withdrawal penalties.

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All other bankers acceptances, deposit and debt obligations issued by depository institutions would be subject to a 15% haircut, plus undue concentration, if appropriate.

*These include but are not limited to certificates of deposit, deposit notes and bank bills.

If you or any member of the staff have any questions or need additional information, please do not hesitate to call E.L. Alvey at 201 902-4382.

Very truly yours,

Paul J. Isaac /asg
Paul J. Isaac
Chairman
Capital Committee

PJI:mq
Attachments

1814/4444A