



SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

DIVISION OF  
MARKET REGULATION

May 14, 1980

Ronald J. Consiglio  
Partner  
Deloitte, Haskins & Sells  
One Wilshire Building  
Los Angeles, California 90017

Dear Mr. Consiglio:

This is in response to your letters of July 3, 1978 and January 16, 1979 on behalf of your client, Bateman Eichler, Hill Richards Incorporated ("BEHR"). You ask our interpretation of the acceptability under Rule 15c3-3 under the Securities Exchange Act of certain procedures of BEHR.

I understand the pertinent facts to be as follows: BEHR is a member of the Pacific Securities Depository ("PSD") and a clearing member of the Pacific Stock Exchange. BEHR maintains most of its customer margin securities at PSD and secures its customer loans with these securities. BEHR borrows on these securities from an institution (the "bank") which is also a PSD member. The contract between BEHR and PSD allows only this specific bank access to the securities in the BEHR bank loan ("pledge") account at PSD. PSD must follow the instructions of the bank regarding disposition of all securities in this account.

Securities deposited at PSD can be credited to various PSD accounting locations or categories depending on the depositor's instructions. Movements between these securities locations do not involve the physical movement of securities but are bookkeeping movements only. There is a charge levied by PSD for each bookkeeping movement.

In order to minimize the PSD charges for daily bookkeeping movements, upon depositing securities, BEHR instructs PSD to credit its pledge account. Details of the securities positioned in this account are contained in the PSD Member Positions Report which PSD sends daily to BEHR and the bank. BEHR has agreed to hypothecate certain of these securities with the bank.

BEHR and the bank have entered into an agreement which specifically states that only the securities which BEHR has

indicated in a daily written communication (which is acknowledged by the bank as being hypothecated) can be used by the bank in event of a liquidation of BEHR. Securities which are considered customer fully-paid and excess margin securities and which may not be reached by the bank in the event of a liquidation are also positioned in the pledge account but are excluded from hypothecation with the bank by the daily written communication.

The agreement between the bank and BEHR, dated May 11, 1978 sets forth a system for determining the number of units of each security issue in the pledge account that will be considered bank loan collateral and the number to be considered segregated customer fully-paid or excess margin. The number of units the bank and BEHR consider as pledged depends on manual alterations by BEHR of the PSD report. If all the units shown in the pledge account are to be used for bank loan collateral, no alterations will be made to the report. If customer fully-paid or excess margin securities are in the pledge location (which shares may not be pledged), BEHR crosses out the printed shares in the pledge column of the PSD report and writes between the "net" column and the "unclassified" column the remaining number of shares, if any, which the bank may use as bank loan collateral.

The difference between the original printed number of units and the number of units written in by BEHR is the unit amount of the customer fully-paid or excess margin securities not to be used for bank loan collateral but to be considered segregated customer securities. This report is forwarded in duplicate to the bank on a daily basis. One copy is stamped by the bank and returned to BEHR. The stamped copy will serve as acknowledgement of units pledged to the bank and units held for segregation purposes by the bank for BEHR's customers.

When BEHR changes the printed units in the pledge column on the member position report, BEHR also changes the market value to reflect the number of units remaining in the pledge location. BEHR crosses out the original market value and puts directly under that value the market value of only those units being pledged to the bank. BEHR borrows based on this adjusted bank loan collateral figure. BEHR attaches to this report an adding machine tape of the value of each individual security position being pledged. This tape serves as proof of the new bank loan collateral figure.

BEHR also provides the bank on a daily basis with a status report of the collateral physically held by the bank; this report shows each security and the total market value of the securities in each account. These status reports provide the bank with the current market value of the securities it physically holds for bank loan collateral.

Additionally, BEHR provides a cover sheet to these reports which summarizes BEHR's borrowing capabilities by security location. This summary report also states the value of the securities in the PSD pledge loan account which is unavailable as collateral. The bank and BEHR have agreed that at the close of each business day, each will have a copy of the cover sheet and all the supporting reports as described above.

In the event of liquidation of the assets of BEHR, the information on the most recent of these reports will be final as to which securities are bank loan collateral and which are fully-paid securities or excess margin securities segregated pursuant to Rule 15c3-3(b). You have stated that the bank has agreed to do everything "within its power" to expedite the delivery of the fully-paid securities or excess margin securities to BEHR or its trustees.

You are asking whether the customer securities in the PSD pledge account (which account is in the control of the bank), are in the "control" of BEHR for purposes of Rule 15c3-3(b) which requires physical possession or control of all fully-paid securities and excess margin securities carried by a broker or dealer for the account of customers. Securities under the control of a broker or dealer are deemed by Rule 15c3-3(c)(5) to be securities which:

"are in the custody or control of a bank as defined in Section 3(a)(6) of the Act, the delivery of which securities to the broker or dealer does not require the payment of money or value and the bank having acknowledged in writing that the securities in its custody or control are not subject to any right, charge, security interest, lien or claim of any kind in favor of a bank or any person claiming through the bank."

Ronald J. Consiglio  
Page Four

It is the view of the Division if BEHR meets all of the following conditions, the Division of Market Regulation would raise no question and recommend no action be taken against BEHR if it deems those securities determined unavailable for collateral and in the custody of PSD to be in BEHR's control under the circumstances described above, although PSD is unaware of which securities are considered by the bank and BEHR to be pledged to the bank and which are considered to be held for segregation purposes by the bank for BEHR's customers:

1. The agreement between BEHR and the bank must contain the language required of clearing agency subcustodians pursuant to subparagraph (g) of Rule 15c2-1 under the Securities Exchange Act, that the bank will not for any reason, including the assertion of any claim, right or lien of any kind, refuse or refrain from promptly delivering securities to BEHR which have been determined unavailable for collateral;
2. BEHR must obtain an opinion of counsel that the agreement with the bank is enforceable against the bank according to its terms and the understanding of the agreement contained in this letter;
3. BEHR must meet all the other applicable conditions of Rule 15c3-3.

Very truly yours,



Michael A. Macchiaroli  
Branch Chief

Muir Atherton  
Pacific Securities Depository