of its contribution to the total cost of the project.

(2) The expenditure of funds under this subpart may be applied only to projects for which a proposal has been evaluated under paragraph (b) of this section and approved by the Secretary, except that up to $25,000 each fiscal year may be awarded to a state out of the state's regular apportionment to carry out an ''enforcement agreement.'' An enforcement agreement does not require state matching funds.

(f) *Prosecution of work.* All work must be performed in accordance with applicable state laws or regulations, except when such laws or regulations are in conflict with Federal laws or regulations such that the Federal law or regulation prevails.

§ 253.23 Other funds.

(a) *Funds for disaster assistance.* (1) The Secretary shall retain sole authority in distributing any disaster assistance funds made available under section 308(b) of the Act. The Secretary may distribute these funds after he or she has made a thorough evaluation of the scientific information submitted, and has determined that a commercial fishery failure of a fishery resource arising from natural or undetermined causes has occurred. Funds may only be used to restore the resource affected by the disaster, and only by existing methods and technology. Any fishery resource used in computing the states' amount under the apportionment formula in § 253.21(a) will qualify for funding under this section. The Federal share of the cost of any activity conducted under the disaster provision of the Act shall be limited to 75 percent of the total cost.

(2) In addition, pursuant to section 308(d) of the Act, the Secretary is authorized to award grants to persons engaged in commercial fisheries, for uninsured losses determined by the Secretary to have been suffered as a direct result of a fishery resource disaster. Funds may be distributed by the Secretary only after notice and opportunity for public comment of the appropriate limitations, terms, and conditions for awarding assistance under this section. Assistance provided under this section is limited to 75 percent of an uninsured loss to the extent that such losses have not been compensated by other Federal or State programs.

(b) *Funds for interstate commissions.* Funds authorized to support the efforts of the three chartered Interstate Marine Fisheries Commissions to develop and maintain interstate fishery management plans for interjurisdictional fisheries will be divided equally among the Commissions.

§ 253.24 Administrative requirements.

Federal assistance awards made as a result of this Act are subject to all Federal laws, Executive Orders, Office of Management and Budget Circulars as incorporated by the award; Department of Commerce and NOAA regulations; policies and procedures applicable to Federal financial assistance awards; and terms and conditions of the awards.

PART 255—[REMOVED]

4. Under the authority of 46 U.S.C. 1271–1279, part 255 is removed.

[FR Doc. 96–10664 Filed 4–30–96; 8:45 am]

BILLING CODE 3510–22–P

COMMODITY FUTURES TRADING COMMISSION

17 CFR Part 1

Early Warning Reporting Requirements, Minimum Financial Requirements, Prepayment of Subordinated Debt, Gross Collection of Exchange-Set Margin for Omnibus Accounts and Capital Charge on Receivables From Foreign Brokers

AGENCY: Commodity Futures Trading Commission.

ACTION: Final rules.

SUMMARY: Rule 1.12 of the Commodity Futures Trading Commission (Commission or CFTC) sets forth the financial early warning reporting requirements for futures commission merchants (FCMs) and introducing brokers (IBs), which are designed to afford the Commission and industry self-regulatory organizations (SROs) sufficient advance notice of a firm's financial or operational problems to take such protective or remedial action as may be needed to assure the safety of customer funds and the integrity of the marketplace. The Commission has determined to adopt amendments to Commission Rule 1.12, applicable to FCMs only, that will: amend paragraph (g) to require the reporting of a reduction in net capital of 20 percent or more within two business days and a planned reduction in excess adjusted net capital of 30 percent or more two business days prior thereto, and to make that paragraph applicable to all FCMs, rather than just those FCMs subject to the risk assessment reporting requirements of Commission Rule 1.15; require reporting of a margin call that exceeds an FCM's excess adjusted net capital which remains unanswered by the close of business on the day following the issuance of the call; and require reporting by an FCM when-ever its excess adjusted net capital is less than six percent of the maintenance margin required to support positions of noncustomers carried by the FCM, unless the noncustomer is itself subject to the Commission's minimum financial requirements for an FCM or the Securities and Exchange Commission's (SEC's) minimum financial requirements for a securities broker-dealer (BD).

The Commission has also determined to adopt amendments to: Rules 1.17(a)(1)(i) and (ii) to (a) increase the minimum required dollar amount of adjusted net capital for FCMs from $50,000 to $250,000, (b) increase the minimum required dollar amount of adjusted net capital for IBs from $20,000 to $30,000, and (c) make the amount of adjusted net capital required by a registered futures association for its member FCMs and IBs an element of the Commission's minimum financial requirements for FCMs and IBs; Rule 1.17(h)(2)(vii) with respect to the procedure to obtain approval for prepayment of subordinated debt; and Rule 1.58, which governs gross collection of exchange-set margins for omnibus accounts, to make it applicable to omnibus accounts carried by FCMs for foreign brokers. The Commission believes that these amendments will conform the Commission's rules with those of SROs and therefore should not require changes in the operations of most firms. In addition, the Commission has determined that the five percent capital charge for unsecured receivables from a foreign broker will not apply where the receivables represent deposits required to maintain futures or options positions, the foreign broker has been granted comparability relief under Commission Rule 30.10, and the asset is held in accordance with the relevant grant of relief under Rule 30.10 at the foreign broker, with another foreign broker that has been granted comparability relief under Commission Rule 30.10, or at a depository in the same jurisdiction as either foreign broker in accordance with Commission Rule 30.7.

EFFECTIVE DATE: May 31, 1996.

FOR FURTHER INFORMATION CONTACT: Paul H. Bjarnason, Jr., Chief Accountant, or Lawrence B. Patent, Associate Chief Counsel, Division of Trading and Markets, Commodity Futures Trading Commission, 1155 21st Street, N.W., Washington, D.C. 20581; telephone (202) 418–5459 or 418–5439.

SUPPLEMENTARY INFORMATION:

I. Early Warning Rules

A. Reportable Events in General

The Commission has required each FCM [1] to report to the Commission and to the FCM's designated self-regulatory organization (DSRO) certain events pertaining to the FCM's financial condition, the FCM's procedures for safeguarding customer and firm assets, and its ability to monitor its financial condition through an appropriate system of records and reports. The purpose of such reporting is to make the Commission and the FCM's DSRO aware of circumstances that have or potentially could have a negative impact on the FCM's ability to carry on normal business operations consistent with the Commission's prudential requirements and pose a potential threat to customer funds or the FCM's financial integrity. Receipt of such notices results in a heightened degree of surveillance over the FCM by the Commission and the DSRO. The events to be reported include undercapitalization, the FCM's adjusted net capital being below its early warning level (*i.e.,* 150 percent of the minimum required), failure to maintain current books and records, the existence of material inadequacies in the FCM's accounting systems or internal controls, and the issuance of a margin call exceeding the FCM's adjusted net capital. Collectively, these are known as the Commission's early warning reporting requirements and are set forth in Rule 1.12. With respect to notices relative to reductions in capital, one purpose of this rulemaking has been to harmonize required notices to the SEC and relevant futures and securities SROs.

B. Background of This Rulemaking

On March 1, 1994, the Commission published proposed Risk Assessment Rules for Holding Company Systems, 59 FR 9689. Certain portions of these proposals were adopted as final rules by the Commission. 59 FR 66674 (Dec. 28, 1994). The proposed risk assessment rules generally would have required, *inter alia,* an FCM to notify the Commission of certain events or transactions that would reduce or potentially reduce the FCM's net capital. These ''triggering'' events were originally proposed to be included in a new Rule 1.15 as part of the risk assessment reporting rules. However, several of the commenters on the risk assessment proposals suggested that the reporting of certain of these triggering events should more appropriately be part of the Commission's early warning reporting system set forth in Rule 1.12, and the Commission agreed. Therefore, when the Commission adopted as part of the risk assessment rulemaking one of the triggering provisions relating to declines in an FCM's adjusted net capital, that provision was adopted as Rule 1.12(g) instead of as a provision of Rule 1.15, and was made applicable only to those FCMs which are required to file reports under Rule 1.15.[2]

Certain commenters on the risk assessment proposals had suggested that the notice provision relating to declines in capital should be applicable to all FCMs, not just those subject to the risk assessment rules. The Commission agreed, but was concerned that FCMs which believed that they were not subject to the risk assessment rules may not have availed themselves of the opportunity to comment upon the Commission's March 1994 risk assessment proposals, including the provision adopted as Rule 1.12(g). Therefore, the Commission adopted Rule 1.12(g) in December 1994 as applicable only to those FCMs subject to the risk assessment rules and at the same time proposed to amend Rule 1.12(g) to make the reporting of capital declines applicable to all FCMs. 59 FR 66822 (Dec. 28, 1994). In the same Federal Register release which announced the proposed amendment to Rule 1.12(g), the Commission also proposed to make certain other changes to the early warning system as an adjunct to its risk assessment initiative and in response to comments received on the March 1994 risk assessment rule proposals which would: (1) require an FCM to report a margin call that exceeds its excess adjusted net capital and remains unanswered by the close of business on the day following the issuance of the call (proposed Rule 1.12(f)(4)); and (2) require an FCM to report whenever its excess adjusted net capital is less than six percent of the maintenance margin required to support proprietary and noncustomer positions carried by the FCM (proposed Rule 1.12(f)(5)).

The Commission originally permitted 30 days for public comment on the proposed amendments to Rule 1.12 and it extended the comment period for an additional 30 days in response to a request from the Securities Industry Association (SIA). 60 FR 7925 (Feb. 10, 1995). The Commission received six written comments on these proposals, including two from contract markets (Chicago Board of Trade (CBT) and Chicago Mercantile Exchange (CME)), two from trade associations (Futures Industry Association (FIA) and SIA), one from an FCM, Bielfeldt & Company (Bielfeldt), and one from an associated person, Alvin L. Goldberg. The Commission's Division of Trading and Markets (Division) also received two letters from the Intermarket Financial Surveillance Group (IFSG),[3] dated February 22 and April 8, 1996, respectively, which bear directly upon one of these proposals and have been considered along with the other comment letters.

The Commission has carefully considered the comments received. The Commission has determined to adopt the proposed amendment concerning unanswered margin calls as proposed. The Commission has also determined, based upon a review of the comments and its own reconsideration of the proposal, that the provision of the early warning system for FCMs requiring a comparison of excess adjusted net capital to six percent of the maintenance margin level will only apply to those positions carried by an FCM on behalf of a noncustomer that is not itself subject to the Commission's minimum financial requirements for an FCM or the minimum financial requirements of the SEC for a BD. The Commission is therefore not adopting Rule 1.12(f)(5) as proposed, which would have applied six percent of the maintenance margin level to all positions held in noncustomer and proprietary accounts. The Commission has further determined to modify slightly the standards in Rule 1.12(g) concerning notice of substantial declines in capital in light of the comments received, particularly the IFSG letters, and its own reconsideration of the issue. The Commission has also clarified certain matters in response to issues raised in the comment letters, as discussed more fully below.

C. Reductions in Capital

As noted above, the Commission in December 1994 added to the list of

[1] Rule 1.12 also requires certain reports from FCMs, IBs, and exchange clearing organizations. The rule amendments that have been adopted relate only to reporting by FCMs. No changes have been made with respect to reporting requirements imposed on FCM applicants, IBs or IB applicants, or clearing organizations.

[2] The balance of the proposed trigger event provisions remains under consideration by the Commission.

[3] The IFSG was formed in 1988 to provide a coordinating body to address financial surveillance issues relevant to both futures and securities markets. It includes representatives of most of the principal commodity and securities exchanges as well as the National Futures Association (NFA) and the National Association of Securities Dealers, Inc. Staff members of the CFTC and of the SEC frequently attend IFSG meetings as observers.

reportable events under Rule 1.12 a new paragraph (g), requiring that certain FCMs (*i.e.*, those FCMs required to file risk assessment reports) report capital declines which may not necessarily result in the FCM being undercapitalized or its capital declining below early warning levels, but which are sufficiently material to the FCM's regulatory capital to warrant enhanced monitoring by the Commission and the FCM's DSRO.[4]

The event currently required to be reported under Rule 1.12(g) is the occurrence of any transaction or condition that results in a reduction of more than 20 percent in the adjusted net capital of an FCM from that reported in the most recent financial report filed with the Commission pursuant to Commission Rule 1.10.[5] The rule draws a distinction, with respect to when the event must be reported, between those events occurring in the normal course of business and those which are extraordinary. If the decline in adjusted net capital is due to activities in the normal course of an FCM's business, the reduction is to be reported within two business days following the event. These events are not normally planned for in advance, such as operating losses, proprietary trading losses or increased charges against net capital. However, where a transaction or series of transactions is planned to be taken which will reduce adjusted net capital by more than 20 percent, the notice must be filed at least two business days in advance of the transaction or series of transactions.[6] This would permit Commission or DSRO staff to make further inquiries concerning the transaction before the transaction is effected to assure that the FCM has adequately considered the effect of the transaction on its overall liquidity. Ideally, an explanation would be included to facilitate this process. The rule does not provide for Commission approval or disapproval of the transaction prior to the FCM effecting the transaction, nor does it provide a means for the Commission to delay or prevent the FCM from carrying out the transaction.[7]

The filing under Rule 1.12(g) is to be made, in accordance with Rule 1.12(h), with the regional office of the Commission with which the FCM normally files its financial reports under Rule 1.10, with the principal office of the Commission in Washington, D.C., with the FCM's DSRO and with the SEC if the FCM is also registered as a BD. Rule 1.12(g) also provides that, following receipt of a notice from an FCM, the Director of the Division, or the Director's designee, may request additional information concerning the effect of the reported event on the FCM's financial or operational condition. The FCM is required to provide such additional information within three business days, or sooner if the Division believes prompter filing is needed to address the condition causing the filing of the early warning notice and so requests.

As adopted in December 1994, Rule 1.12(g) applies only to those FCMs which are required to file reports with the Commission under the risk assessment rules. Several commenters on the Commission's March 1994 risk assessment proposals, including FIA and NFA, suggested that the reporting requirement now in paragraph (g) be made applicable to all FCMs, not just those required to report under Rule 1.15. The Commission agreed that this reporting requirement serves to alert the Commission and DSRO to potential problems resulting from transactions that affect an FCM directly and therefore should not be limited to those FCMs subject to the risk assessment rules. Since FCMs that believed they were not subject to the risk assessment rules may not have taken the opportunity to comment on the Commission's March 1994 risk assessment rule proposals, the Commission determined to publish these proposed changes to Rule 1.12(g) for comment.

All of the commenters on the Commission's December 1994 proposals addressed the Commission's proposal concerning Rule 1.12(g). Two commenters expressed support for the extension of Rule 1.12(g) to all FCMs. Three commenters noted that several regulators and SROs had similar, but slightly different, requirements in this area. They further pointed out that the IFSG was attempting to develop a consensus on how to harmonize the various requirements directed at the same types of reporting and requested that the Commission not adopt its proposals until the IFSG completed its study. One of these commenters, FIA, suggested in the alternative that the Commission adopt a ''no-action'' position to permit an FCM to follow a related rule of its DSRO or the New York Stock Exchange, Inc. (NYSE), as elected by the FCM. The IFSG reported on its harmonization efforts in its letters to the Division dated February 22 and April 8, 1996 and stated that the Commission and SEC should adopt similar rules which would require two business days prior notice when excess adjusted net capital is to be reduced 30 percent or more and notice within two business when net capital has been reduced by 20 percent or more.[8]

As noted above, the Commission requested comment as to whether Rule 1.12(g) should establish a mechanism by which the Commission could delay or prevent an FCM from carrying out planned transactions that would reduce adjusted net capital by more than 20 percent. Three commenters stated that the Commission should not be able to delay or prevent capital reductions. A fourth commenter, SIA, stated that for firms dually registered as FCMs and BDs, only the SEC should have such authority, but it supported CFTC authority to delay or prevent capital reductions for other FCMs (*i.e.*, those not also registered as BDs). Although it did not directly address the question posed by the Commission, the FCM commenter, Bielfeldt, stated that no notice under Rule 1.12(g) should be required with respect to capital reductions resulting from planned transactions. Another commenter, Mr. Goldberg, expressed his belief that the capital rules as written do not require

[4] There are approximately 190 FCMs required to file risk assessment reports, and the extension of Rule 1.12(g) would cover the remaining FCMs, approximately 70 firms.

[5] Certain exchanges have a similar requirement. The rule amendment whose adoption is announced herein is intended to induce all SROs to conform their similar rules to the Commission requirement. *See* CME Rule 972A; CBT Rule 285.03; New York Mercantile Exchange Rule 2.14(d) and Clearing Rule 9.22(c)(i) and (ii); Commodity Exchange, Inc. Rule 7.08(a); Coffee, Sugar and Cocoa Exchange, Inc. Clearing Rule 302(c)(i); Kansas City Board of Trade Rule 1311.00; Kansas City Board of Trade Clearing Corporation Rule 8.01(c); and Minneapolis Grain Exchange Rule 2088.00.

[6] The SEC also has a similar rule, Rule 240.15c3–1(e)(1), 17 CFR 240.15c3–1(e)(1)(1995), which requires a BD to provide notice two business days prior to withdrawals of equity capital that on a net basis exceed in the aggregate in any 30 calendar day period, 30 percent of the firm's excess net capital, or two business days after such withdrawals during any 30 calendar day period exceed 20 percent of the firm's excess net capital.

[7] As more fully discussed below, the Commission requested comment as to whether Rule 1.12(g) should establish a mechanism by which the Commission could delay or prevent an FCM from carrying out the transaction. The SEC has authority to restrict capital withdrawals for up to twenty business days under certain conditions. 17 CFR 240.15c3–1(e)(3)(1995).

[8] IFSG's first letter dated February 22, 1996, which was superseded by its April 8, 1996 letter, recommended that the notices be made 48 hours, rather than two business days, prior to or following the event, and that such notices be based upon net capital declines in either situation, rather than upon a decline in excess adjusted net capital with respect to prior notice. The prior notice rule adopted herein is the same as that of the SEC adjusted to apply to FCMs and the subsequent notice in the same as that required by the NYSE so adjusted. FCMs that are BDs will continue to have to file any additional notices required by the SEC which in the case of post-reduction notices may include some notices triggered by haircuts.

firms to establish systems to monitor capital on a day-to-day basis; in his view, it is sufficient if a firm can, at a later date, demonstrate that it was in compliance on any date. Therefore, Mr. Goldberg believes that the effect of planned transactions on a firm's capital would not be readily determinable, rendering a firm incapable of providing early warning with respect to such transactions.

There were two other comments related to the proposed amendment of Rule 1.12(g). Two commenters requested clarification that notice under the rule would not be required with respect to repayment or prepayment of subordinated debt, since separate notice of such events and DSRO approval is already required. Another commenter stated that the calculation used in Rule 1.12(g) should be based upon net capital, as modified by the dollar amount of deficit and undermargined accounts, rather than adjusted net capital.

The Commission has carefully considered these comments and has determined to amend Rule 1.12(g) consistent with the suggestions of the IFSG.[9] The Commission believes that this action will make its rule concerning capital reductions consistent with the SEC's rule and the rules of futures and securities industry SROs in this area. The IFSG's letters were jointly addressed to the Division and to the SEC's Division of Market Regulation (DMR) and the Division's staff has been in contact with DMR staff to assure similarity of treatment regarding early warning notices related to capital reductions. The Commission's December 1995 proposals, which are discussed more fully below, as well as the Commission's February 1996 proposals,[10] were intended to conform Commission minimum financial and related reporting requirements with those of the SROs and SEC in various areas, as recommended by several participants in the Commission's roundtable on capital issues held on September 18, 1995. A uniform approach among the Commission, SEC and the SROs with respect to notices of major capital reductions should simplify the reporting requirements for FCMs that are also BDs and/or members of more than one futures or securities SRO, eliminating needless inconsistencies among required notices relating to the same types of circumstances, and provide consistent and sufficient information to financial regulators and SROs to permit them to monitor effectively the financial condition of firms under their jurisdiction.

The Commission notes that basing the event requiring notice within two business days upon a decline in net capital rather than adjusted net capital as currently in the rule will require larger reductions to trigger the notice since net capital will normally exceed adjusted net capital. Conversely, since the prior notice requirement will be based upon a decline in excess adjusted net capital rather than adjusted net capital as currently in the rule, smaller reductions could trigger the notice since adjusted net capital will necessarily exceed excess adjusted net capital, despite the fact that the percentage decline required to trigger prior notice has been increased from 20 to 30 percent. The Commission believes that it has now achieved a balanced approach in this area that implements its ongoing resolve to streamline its rules and avoid unnecessary duplication or redundant or inconsistent requirements to the extent consistent with customer protection. It also further harmonizes the Commission's rules with SEC rules and takes account of the ongoing harmonization project of the IFSG.[11]

The Commission has also determined not to establish a mechanism whereby it could delay or prevent an FCM from carrying out planned transactions that would reduce excess adjusted net capital by 30 percent or more. The Commission continues to view the early warning requirements under Rule 1.12 as essentially a mechanism for notification of situations that have or potentially could have a negative impact on a firm's ability to carry on normal business operations consistent with the Commission's prudential requirements and that pose a potential threat to customer funds or a firm's financial integrity. In the case of a planned reduction, the Commission believes that an explanation should accompany the notice. Although the Commission's staff may wish to discuss reported events with the FCM,[12] the Commission does not believe that a formal mechanism to delay or prevent events giving rise to a notice under Rule 1.12(g) is warranted at this time. The Commission currently has the authority to require specific reports from custodians upon the transfer of segregated funds in certain circumstances and also requires 100 percent segregation of customer obligations unlike the SEC that has a more limited requirement. These two authorities make it less likely that there could be a ''run'' on a futures firm or a misappropriation of segregated funds without additional authority to preclude reductions of capital. Moreover, the Commission is aware of the need for regulators to be sensitive to the liquidity needs of a holding company system as a whole consistent with its responsibilities to the regulated entity.

The Commission also wishes to respond to the comments of Bielfeldt and Mr. Goldberg that no notice should be required or can be prepared with respect to capital reductions resulting from planned transactions. As the Commission stated when it published the proposals:

> The Commission's early warning rules relating to an FCM's level of capital contemplate that the FCM will have systems in place to monitor its capital levels and its compliance with the Commission's net capital rules on a day-to-day basis. The Commission requires each FCM to be able to demonstrate its capital compliance at any time and not just on a required formal computation or filing date.[13] Consequently,

[9] The IFSG's April 8, 1996 letter made two other suggestions in addition to those referred to above which were that: (1) notice not be triggered by a futures or securities transaction in the ordinary course of business between an FCM and an affiliate where the FCM makes payment to or on behalf of such affiliate for such transaction and then receives payment from such affiliate for such transaction within two business days from the date of the transaction; and (2) an FCM's DSRO have discretion to exempt the FCM from filing notice under Rule 1.12(g) where withdrawals, advances or loans in the aggregate, on a net basis, equal $500,000 or less. The Commission is adopting the former suggestion as a proviso to Rule 1.12(g). As to the second suggestion, Commission staff discussed the issue with an IFSG representative, who stated that it was included in the letter since the SEC rule provides for such exemptions. The IFSG representative further indicated that such a provision was not an issue of concern to the futures industry members of IFSG so the Commission is not including it in Rule 1.12(g).

[10] 61 FR 7080 (Feb. 26, 1996). These proposals concerned the financial reporting cycle and the debt-equity ratio requirements for FCMs and IBs.

[11] For an FCM dually registered as a BD and taking advantage of the option available under Commission Rule 1.10(h) to file a copy of its Financial and Operational Combined Uniform Single (FOCUS) Report in lieu of Form 1–FR–FCM (which includes about one-half of all FCMs), the calculation for subsequent notice would be based upon ''tentative net capital'' as set forth in SEC Rule 240.15c3–1, i.e., net capital before securities haircuts, and the calculation for prior notice would be based upon ''excess net capital.'' The Commission's definition of net capital and the SEC's definition of tentative net capital, as well as the Commission's definition of excess adjusted net capital and the SEC's definition of excess net capital, are for practical purposes the same.

[12] The Commission notes that Rule 1.12(g)(3) provides that the Director of the Division or the Director's designee may require an FCM filing a notice under Rule 1.12(g) to furnish additional information. The Commission believes that it is important to maintain this flexibility and this is another reason why early warning notices should be filed with the Commission as well as the DSRO and not only with the latter as Bielfeldt suggested.

[13] See Commission Rules 1.17(a)(3)–(5) and 1.18(b), 17 CFR 1.17(a)(3)–(5) and 1.18(b) (1995).

the effect of planned transactions on net capital should be readily determinable.

The Commission further notes that since it issued these proposals, the failure of Barings PLC has occurred. That failure only reinforces the need for FCMs to have robust internal controls and capital monitoring systems that permit a firm to assess its financial position on a day-to-day, if not more frequent, basis.

In response to the request of two of the commenters noted above, the Commission wishes to make clear that Rule 1.12(g) does not require separate notice with respect to repayment or prepayment of subordinated debt since an FCM must always get approval for prepayment of subordinated debt from its DSRO as discussed more fully below.[14]

D. Unanswered Margin Calls

As part of the March 1994 risk assessment rule proposals, the Commission had proposed Rule 1.15(b)(2)(iii), which would have required an FCM to notify the Division whenever aggregate cumulative losses in all noncustomer accounts exceeded the greater of: (A) in any 30-day period, 10 percent of the last reported consolidated stockholders' equity of the FCM's parent or $50 million, or (B) in any 12-month period, 20 percent of the last reported consolidated stockholders' equity of the FCM's parent or $100 million.[15] This proposal was opposed by several commenters. Some of the commenters suggested that, as an alternative, an FCM be required to notify the Commission within two business days after a margin call to a noncustomer remains outstanding for two business days, if the margin call exceeds 20 percent of the FCM's adjusted net capital.

In response to these comments, the Commission determined in December 1994 to propose Rule 1.12(f)(4) which would require an FCM to file an early warning notice when a margin call on a customer, noncustomer or omnibus account that exceeds the firm's excess adjusted net capital is not answered by the close of business on the day following the day the call is made. The Commission's proposal would permit FCMs to take into account favorable market moves in determining whether the margin call would be required to be reported under this rule.[16]

For purposes of proposed Rule 1.12(f)(4), a margin call would mean any deposit of funds required by the FCM to margin, guarantee or secure a futures or commodity option position. Thus, if, with respect to an exchange-traded contract, the FCM requires a deposit in excess of the minimum required pursuant to exchange rules, that greater amount would be the amount used in determining whether a call has been collected from an account holder. Although exchanges may exempt firms from the requirements of Commission Rule 1.12(f)(3), which requires notice of issuance of a margin call in excess of a firm's entire adjusted net capital, the Commission proposed not to permit the granting of such waivers from the Rule 1.12(f)(4) notice requirement. The Commission also requested additional comment, however, on the originally proposed trigger event for which Rule 1.12(f)(4) was proposed as an alternative.[17]

The contract market and trade association commenters addressed proposed Rule 1.12(f)(4). CBT supported the proposal. CME, FIA and SIA stated that the rule should be based upon the exchange minimum maintenance margin level only, since such a rule could otherwise be a disincentive for FCMs to establish higher internal margin requirements. FIA and SIA also requested that the Commission allow more time to meet a margin call before notice is required if foreign customers are involved. CBT and CME urged the Commission to repeal Rule 1.12(f)(3), which requires an FCM to file a notice when an account is undermargined by an amount in excess of the FCM's adjusted net capital, since it is little used and similar to the proposal. FIA suggested two clarifications: (1) That the Commission state that a margin call is usually issued on the day following the day the account becomes undermargined; and (2) that the provision be applied to all commodity interest accounts subject to margining. FIA and SIA also requested that the Commission define ''excess adjusted net capital.''

The Commission has carefully considered these comments and has determined to adopt Rule 1.12(f)(4) as proposed. As to whether the minimum margin standard in the rule should be the exchange minimum level or any higher amount set by the FCM, the Commission believes that FCMs establish margin requirements for accounts based upon an assessment of the creditworthiness of the account owner and that a Rule 1.12(f)(4) notice requirement should have negligible impact in the context of margin requirements intended to safeguard a firm's financial position. Further, if the Commission adopted the view of certain commenters that the exchange minimum maintenance margin level is the appropriate level for purposes of Rule 1.12(f)(4) and an FCM set an account's maintenance margin level higher than the minimum requirement of an exchange, the FCM would be required to monitor the impact of the lower exchange minimum requirement for purposes of Rule 1.12(f)(4). The Commission believes that such a requirement could be more costly and confusing to keep track of than simply requiring an FCM to treat a margin call for the account as a margin call under Rule 1.12(f)(4).

Concerning the comment that more time be allowed to meet a margin call if foreign customers are involved, the Commission is not persuaded that this would be appropriate. As far back as the October 1987 market break, the Division noticed a disproportionate incidence of customer defaults and liquidations attributable to foreign traders. FCMs were urged to establish procedures to assure that they obtain adequate security from foreign customers to protect against the potential for price fluctuations to result in aberrant margin calls that could not be readily satisfied by such customers and that, for the FCM, could be unduly costly or impossible to recover were legal action against the customer ultimately required.[18] The Commission believes that the events that have occurred since 1987, including the growing internationalization of the futures markets, and the Commission's determination, as discussed below, to require gross collection of exchange-set margin for all omnibus accounts, including those originated by foreign brokers, lead to the conclusion that margin calls attributable to foreign traders should not be given preferential treatment in the context of the early warning notice requirement of Rule 1.12(f)(4).

In response to FIA's suggestions, the Commission wishes to make clear that a margin call is usually issued on the business day following the business day the account becomes undermargined and that Rule 1.12(f)(4) as proposed and adopted ''applies to all accounts carried by the futures commission merchant

[14] *See* Commission Rules 1.17(h)(2)(vii) and (viii), 17 CFR 1.17(h)(2)(vii) and (viii) (1995); CFTC Interpretative Letter No. 85–17, [1984–1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶22,738 (Sept. 10, 1985).

[15] 59 FR 9689, 9706 (March 1, 1994).

[16] 59 FR 66822, 66823–24.

[17] *See* proposed Rule 1.15(b)(2)(iii) in the March 1994 risk assessment proposals, 59 FR 9689, 9706.

[18] Follow-up Report on Financial Oversight of Stock Index Futures Markets During October 1987, CFTC Division of Trading and Markets, at 84 (Jan. 6, 1988).

* * * that are subject to margining * * *.'' As to the term ''excess adjusted net capital,'' this means an FCM's adjusted net capital less its required minimum adjusted net capital computed in accordance with Commission Rule 1.17.[19] The Commission further wishes to make clear that the notice required by Rule 1.12(f)(4) must include account name, date of margin call, amount of margin call and the FCM's excess adjusted net capital. The Commission also believes that Rule 1.12(f)(3) referred to above, although somewhat similar to Rule 1.12(f)(4), should continue as a separate early warning notice requirement.

E. Maintenance Margin Factor

Some commenters on the Commission's March 1994 risk assessment proposals also suggested that, in lieu of adopting the proposal referred to above concerning the reporting of losses in noncustomer accounts, the Commission amend Rule 1.12 to add an early warning reporting requirement to require an FCM to report to the Commission whenever its excess adjusted net capital is less than six percent of the maintenance margin requirement applicable to positions in proprietary and noncustomers' accounts. These commenters noted that the CME imposes a capital requirement on an informal basis on its clearing members that factors in a percentage of proprietary and noncustomers margin requirements. The Commission determined to propose an amendment to Rule 1.12 in December 1994 in line with the commenters' suggestions.

All of the commenters on the December 1994 proposals addressed this provision and stated that proprietary positions are subject to haircuts and thus should not be included in the calculation for an early warning notice requirement.[20] The trade association commenters also stated that positions held by noncustomers who are subject to capital requirements of the Commission, or of another regulator or an SRO, either domestic or foreign, should not be included in the calculation required by Rule 1.12(f)(5).

The Commission has reconsidered its proposal in light of these comments. As noted above, the proposal responded to comments on the March 1994 risk assessment proposals which apparently misread the CME's requirements, since the CME rule only adds a percentage of noncustomer margin. The Commission recognizes that proprietary positions are already accounted for in the minimum financial rule through haircuts; however, noncustomer positions are not and neither are they factored into the minimum financial requirement based upon four percent of customer funds. Based upon the comments and its reconsideration of the issue, the Commission has determined not to include proprietary accounts as a factor in determining whether notice is required under Rule 1.12(f)(5).[21] However, noncustomer accounts will be included in the calculation under Rule 1.12(f)(5), unless the noncustomer is itself subject to the Commission's minimum financial requirements for an FCM or the SEC's minimum financial requirements for a BD. This is intended to reflect the fact that affiliates rarely retain excess funds at the clearing firm. The Commission will reassess whether this exclusion is appropriate in connection with its further review of the capital rule as a whole.

II. Minimum Financial Requirements for FCMs and IBs

On December 7, 1995, the Commission voted to propose amendments to Rule 1.17 to: (a) Increase the required minimum dollar amount of adjusted net capital for FCMs from $50,000 to $250,000;[22] (b) increase the required minimum dollar amount of adjusted net capital for ''independent'' IBs from $20,000 to $30,000;[23] and (c) make the amount of adjusted net capital required by a registered futures association for its member FCMs and IBs an element of the Commission's minimum financial requirements for FCMs and IBs.[24]

These amendments were proposed in order to permit the Commission to use its authority under Section 6c of the Commodity Exchange Act (Act)[25] to enforce compliance with what are effectively, for the reasons discussed when the proposals were published,[26] the current minimum adjusted net capital requirements applicable to FCMs and independent IBs with the benefit of all of the remedies available to the Commission under the Act for the enforcement of compliance with any provision of the Act and any rule promulgated thereunder.[27] In addition, these amendments would harmonize the Commission's minimum financial requirements for FCMs and independent IBs with the prevailing standards established by NFA rules.[28] The amendments would also support the objective of assuring that FCMs have a substantial commitment to meeting their regulatory obligations to customers, an objective for which an increased requirement appears appropriate given the increase in the amount of funds held by FCMs and the change in the value of the dollar since 1978, the last time the Commission increased the required minimum dollar amount of capital for FCMs.[29] The Commission also believed that the proposed amendments to Rule 1.17 were necessary to clarify its authority to require the transfer of positions at such time as a firm is no longer in compliance with the NFA rule, and to eliminate any confusion that may have existed as to whether the Commission could take action where an FCM's adjusted net capital is below $250,000 yet still at least $50,000,[30] or

[19] *See also* 17 CFR 1.17(d)(3) (1995); Form 1–FR–FCM, page 8, line 24.

[20] Bielfeldt further commented that haircuts on proprietary positions should be eliminated and all accounts should be treated similarly for capital purposes. This comment addresses issues outside of the scope of this rulemaking proceeding.

[21] Because of this determination, the Commission's proposal that maintenance margin with respect to an FCM's proprietary account shall mean the amount of funds the FCM is required to maintain at the clearing organization with its clearing broker, or five percent of the value of the contract, whichever is greater, is moot. The Commission requested comment on that point and CME and Bielfeldt objected to the five percent provision, while CBT thought such a provision should be used only in the absence of margin being set by the exchange or clearing organization.

[22] This proposal would also have the effect of increasing an FCM's ''early warning'' level of adjusted net capital from $75,000 to $375,000 despite the fact that Rule 1.12(b)(1) itself would not be amended.

[23] More than two-thirds of IBs enter into a guarantee agreement with an FCM in accordance with Commission Rules 1.17(a)(2)(ii) and 1.10(j) in lieu of raising their own capital, and thus would be unaffected by the proposed amendment.

[24] These proposals and others discussed below were published at 60 FR 63995 (Dec. 13, 1995).

[25] 7 U.S.C. 13a–1 (1994).

[26] *See* 60 FR 63995, 63996.

[27] Section 6c of the Act authorizes the Commission, whenever it appears that a person has engaged, is engaging, or is about to engage in any act or practice constituting a violation of any provision of the Act or any rule or regulation thereunder, to bring an action to enjoin such act or practice, or to enforce compliance with the Act or any rule or regulation thereunder. However, the Commission does not have the authority to discipline an exchange member for violation of an exchange rule in the absence of the exchange's failure to act, or to enforce compliance with a registered futures association's own rule upon a member thereof. *See* Sections 8c(a)(1) and 17(l)(1) of the Act, 7 U.S.C. 12c(a)(1) and 21(l)(1) (1994).

[28] Commission Rule 170.15, 17 CFR 170.15 (1995), mandates that each person required to register as an FCM become and remain a member of a futures association which provides for the membership therein of such FCM unless there is no registered futures association. NFA is the only registered futures association.

[29] 43 FR 39956, 39972 (Sept. 8, 1978).

[30] On November 24, 1992, the SEC adopted rule amendments to raise its minimum net capital requirements for BDs holding customer funds, which had been $25,000, to $250,000 in stages. The requirement increased to $100,000 effective July 1, 1993, $175,000 effective January 1, 1994 and to the current level of $250,000 effective July 1, 1994. *See* 57 FR 56973, 56990 (Dec. 2, 1992); 17 CFR 240.15c3–1e(a) (1995).

an independent IB's adjusted net capital is below $30,000 yet still $20,000 or more.[31]

Four comment letters were received on the December 1995 proposals, submitted by FIA, NFA, CBT and CME. FIA and NFA supported the proposed amendments to the Commission's minimum financial requirements for FCMs and independent IBs. CBT and CME supported raising the minimum dollar amounts of the Commission's financial requirements to those of the NFA for FCMs and independent IBs, but objected to incorporating all aspects of NFA's minimum financial requirements (*i.e.*, the standards based on number of branches and associated persons (APs)) into the Commission's rules.[32] CBT stated that:

> Many SROs have their own internal rules to determine capital that have been developed to address a specific need identified by that SRO. It can be anticipated that the NFA may develop further capital standards to address the capital needs of the firms for which it is primarily responsible and although all FCMs doing customer business are subject to these requirements, by virtue of being members of the NFA, if such requirements become Commission mandates, there would be a greater responsibility placed on the other DSROs to monitor compliance with what are in essence another organization's internal capital requirements.

The Commission disagrees with this comment. A registered futures association cannot impose a minimum financial requirement for its member FCMs and IBs unless such a rule is approved by the Commission. When the Commission approves such a rule of the registered futures association, the proposed amendment would make that standard an element of the Commission's minimum requirements. Therefore, SROs effectively will be monitoring compliance with the minimum financial requirements for doing Commission-regulated FCM business, not another organization's internal capital requirements.[33]

Based upon a review of the comments and its own consideration of these issues, the Commission has determined to adopt the amendments to Rule 1.17(a) as proposed. The Commission is also adopting conforming amendments to the early warning level of adjusted net capital for FCMs (new paragraph (b)(3) of Rule 1.12), the restrictions on withdrawals of equity capital (new paragraph (e)(1)(iii) of Rule 1.17), and various provisions of Rule 1.17(h) concerning subordinated debt.[34] The Commission further notes that several provisions of Rule 1.17 contain cross-references to Rule 1.17(a)(1)(i)(A) and 1.17(a)(1)(ii)(A), the minimum dollar amount of adjusted net capital for FCMs and independent IBs, respectively. These other provisions of Rule 1.17 restrict or require certain actions if specified levels of adjusted net capital, which in all cases exceed 100 percent of the minimum dollar amount, are breached. Thus, the amendments to Rule 1.17(a)(1)(i)(A) and (a)(1)(ii)(A) will have a corresponding impact on various FCM and independent IB activities or obligations referred to elsewhere in Rule 1.17.[35]

III. Approval of Prepayment of Subordinated Debt

The Commission also proposed in December 1995 to codify a Division ''no-action'' letter[36] by amending Commission Rule 1.17(h)(2)(vii)(C) generally to require submission by an FCM or independent IB of a request for approval of prepayment of subordinated debt only to its DSRO.[37] However, the Commission also proposed that dual approval by the DSRO and the Commission would be required if the requested prepayment would result in a reduction of 20 percent or more of the firm's adjusted net capital.[38]

FIA supported the amendment as proposed, but NFA, CBT and CME each raised objections to a requirement for dual approval by the DSRO and the Commission where prepayments of subordinated debt would reduce a firm's adjusted net capital by at least 20 percent. The commenters stated that DSROs have demonstrated the capability to competently handle prepayment of subordinated debt during the past ten years of the no-action period. CME stated that a firm will be required to provide notice of a decrease of 20 percent or more in adjusted net capital pursuant to Rule 1.12(g), as discussed above. CBT recommended that the Commission make clear that a prepayment of subordinated debt that results in a decrease of 20 percent or more in adjusted net capital constitutes a reporting event to the Commission.[39] NFA recommended that approval of such prepayment should only be required by the DSRO, which in turn should be required to provide the Commission with notice of any such approvals.

The Commission has considered this issue in light of the comments received and the other rule amendments it is announcing herein, particularly Rule 1.12(g) discussed above. The Commission believes that dual approval by the DSRO and the Commission need not be required for prepayment of subordinated debt, even if such prepayment would reduce an FCM's or independent IB's net capital by 20 percent or more or its excess adjusted net capital by 30 percent or more. In such cases, however, the DSRO must immediately provide the Commission with a copy of any notice of approval of prepayment of subordinated debt issued to an FCM or an independent IB.[40]

IV. Gross Collection of Exchange-Set Margins

The Commission also proposed in December 1995 to amend Rule 1.58, which governs gross collection of exchange-set margin for omnibus accounts, to make it applicable to omnibus accounts carried by FCMs for foreign brokers. The Commission made this proposal because, in view of the

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[31] The Commission's minimum dollar amount of adjusted net capital for independent IBs has remained unchanged at $20,000 since 1983, when rules governing IBs were first adopted, so the change in the dollar's value since that time justifies an increase to $30,000 for the minimum amount. 48 FR 35248 (Aug. 3, 1983).

[32] NFA minimum financial requirements for FCMs and independent IBs based upon the number of branches and APs are discussed in the proposing release, 60 FR 63995, 63997.

[33] All SROs are required to have in effect and enforce rules approved by the Commission prescribing minimum financial and related reporting requirements for member FCMs and IBs. Such requirements must be the same as, or more stringent than, those contained in Commission Rules 1.10 and 1.17. *See* Commission Rule 1.52, 17 CFR 1.52 (1995).

[34] *See* 60 FR 63995, 63997.

[35] The other provisions of Rule 1.17 referred to herein are discussed at 60 FR 63995, 63996.

[36] CFTC Interpretative Letter No. 85–17, [1984–1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,738 (Sept. 10, 1985).

[37] In those rare instances where the registrant is not a member of any SRO (which would mean that it could not handle customer business), such a request would be submitted to the Commission.

[38] The Commission made clear when it proposed this amendment that if a firm's subordinated debt amounts to 25 percent of its adjusted net capital and the firm wishes to prepay all outstanding subordinated debt and simultaneously enter into new subordinated debt arrangements for the same amount, but with a different maturity date or interest rate, dual approval would *not* be required since there would be no net effect on the firm's adjusted net capital. Similarly, if a firm wanted to convert subordinated debt to paid-in capital, dual approval would not be required so long as such conversion did not result in a reduction of 20 percent or more of the firm's adjusted net capital. 60 FR 63995, 63997–98.

[39] The comment letters referred to the adjusted net capital standard in the proposal. As noted above, the amendments to Rule 1.12(g) as adopted are based upon a reduction in a firm's net capital or excess adjusted net capital.

[40] This requirement is in addition to the current requirement that each DSRO report monthly to the regional office of the Commission nearest to it all actions taken with respect to subordinated loan agreements. Division of Trading and Markets Financial and Segregation Interpretation No. 4–1, ¶ 25, 1 Comm. Fut. L. Rep. (CCH) ¶ 7114A, at 7102 (July 29, 1985).

increasing internationalization of the financial markets, and in particular the increasing use of foreign omnibus accounts, the Commission believed that foreign broker omnibus accounts should be treated in the same manner as omnibus accounts carried for domestic FCMs. The Commission also noted that the proposals would conform Rule 1.58 to the industry practice since, as a result of staff recommendations in rule enforcement reviews and SRO rule changes, all active U.S. contract markets other than the New York Cotton Exchange and the Philadelphia Board of Trade require that FCMs collect margin for omnibus accounts of foreign brokers as well as other domestic FCMs on a gross basis.

FIA, CBT and CME supported the proposed amendment to Rule 1.58 and the Commission has determined to adopt this amendment as proposed.[41] The Commission believes that gross collection of exchange-set margin at the clearing firm materially improves financial control over the positions carried through omnibus accounts.

V. Receivables From Foreign Brokers

Commission Rule 1.17(c)(5)(xiii) requires that an FCM or independent IB, when computing its adjusted net capital, take a charge against its net capital based upon:

> Five percent of all unsecured receivables includable under paragraph (c)(2)(ii)(D) of this section used by the applicant or registrant in computing 'net capital' and which are not receivable from (A) a registered futures commission merchant, or (B) a broker or dealer which is registered as such with the Securities and Exchange Commission.[42]

This provision has been unchanged since it was adopted by the Commission as part of the major overhaul of the minimum financial and related reporting requirements in 1978.[43] In 1978, foreign futures business was totally unregulated and foreign options were banned.

By letter dated January 12, 1996 to the Division, the Joint Audit Committee[44] requested that the Commission exempt from the five percent capital charge set forth in Rule 1.17(c)(5)(xiii) those unsecured receivables from a foreign broker that has been granted ''comparability relief'' under Commission Rule 30.10.[45]

When the Commission adopted Rule 1.17(c)(5)(xiii) in 1978, there were no Part 30 rules and the Commission had little interaction with foreign regulators compared to what it has in that regard today. Indeed, many foreign jurisdictions had no developed regulatory structure for the futures industry at that time. The Commission was therefore concerned that unsecured receivables from foreign brokers represented greater risk to a firm's financial condition than those from a registered FCM or BD, and should be subject to an additional capital charge. The increased cooperation among regulators globally and enhancement of capital standards monitoring today as compared to 1978 justifies a reconsideration of the appropriateness of Commission Rule 1.17(c)(5)(xiii). The Commission also notes that registered FCMs and BDs today may have large exposures in a jurisdiction such as the U.K. and an unsecured receivable from such an FCM or BD would not be subject to a haircut whereas the same receivable from a U.K. affiliate of a U.S. firm would be subject to the five percent charge so the five percent charge is a regulatory rather than a location charge.

Based upon its consideration of this issue, the Commission has determined to add a proviso to Rule 1.17(c)(5)(xiii) such that the haircut will not apply to an unsecured receivable due from a foreign broker if the receivable represents deposits required to maintain futures and commodity option positions (*i.e.*, ''excess'' deposits by an FCM with a foreign broker are still subject to the five percent charge), the foreign broker has been granted comparability relief pursuant to Commission Rule 30.10 and the receivable is held in compliance with the customer funds protection requirements of the relevant Commission order made under Rule 30.10 by the foreign broker itself, with another foreign broker that has been granted comparability relief under Commission Rule 30.10, or at a depository in the same jurisdiction as either foreign broker that would qualify as a depository for funds in accordance with Commission Rule 30.7. Essentially, the Commission is interpreting the existing rule to treat ''Rule 30.10 firms'' akin to a registered FCM, provided the conditions about the nature and location of the receivable are also met. As this relieves a burden on FCMs and independent IBs in computing their adjusted net capital, and follows a request for such relief by the JAC on behalf of the member firms of the SROs, the Commission finds good cause that it is unnecessary to publish this rule amendment for public comment.[46] However, although the Commission is publishing this amendment as a final rule, it would encourage any interested parties to submit comments on this amendment.

VI. Related Matters

A. Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA), 5 U.S.C. 601–611 (1994), requires that agencies, in proposing rules, consider the impact of those rules on small businesses. The rule amendment discussed herein would affect FCMs and independent IBs. The Commission has previously determined that, based upon the fiduciary nature of FCM/customer relationships, as well as the requirement that FCMs meet minimum financial requirements, FCMs should be excluded from the definition of small entity.[47]

With respect to IBs, the Commission stated that it is appropriate to evaluate within the context of a particular rule whether some or all IBs should be considered to be small entities and, if

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[41] A fuller discussion of this issue is set forth in the proposing release. 60 FR 63995, 63998.

[42] This charge relates to funds deposited by an FCM with a foreign broker for clearing transactions on non-U.S. markets, as distinct from the exclusion from current assets for debit/deficit accounts under Rule 1.17(c)(2)(i), where a customer of the FCM has a debt to the FCM.

[43] 43 FR 39956, 39975 (Sept. 8, 1978).

[44] The Joint Audit Committee (JAC) is composed of representatives of all U.S. futures SROs. It was established to coordinate audit and financial surveillance, plans, policies and procedures, particularly with respect to FCMs that are members of more than one SRO. Responsibility for monitoring firms that are members of more than one SRO is allocated among the SROs under a Joint Audit Plan in which all of the exchanges and NFA participate.

[45] 17 CFR 30.10 (1995). Part 30 of the Commission's rules governs foreign futures and options transactions (*i.e.*, commodity interest transactions entered into by a person located in the U.S. on or subject to the rules of a foreign board of trade) and generally requires, among other things, that persons engaged in such transactions for or on behalf of customers located in the U.S. register under the Act. However, the Part 30 rules contain an exemptive provision pursuant to which the Commission may exempt a firm located outside the U.S. from the application of certain of the Commission's rules based upon substituted compliance by the firm with corresponding regulatory requirements of the foreign jurisdiction in areas such as registration, minimum financial requirements, safeguarding of customer funds, record-keeping and reporting requirements, and sales practice standards, and subject to certain conditions primarily related to the protection of customer funds.

The relief is granted to firms designated by a foreign entity such as the United Kingdom Securities and Investments Board or the Association of Futures Brokers and Dealers (U.K.). A listing of these entities is set forth in Appendix C to the Commission's Part 30 rules.

[46] *See* 5 U.S.C. 553(b) (1994). Preliminary review of data related to this charge by the Commission's staff indicates that these receivables are not a substantial asset for most firms. The Commission also notes that its staff will review firms' financial statements to determine if unsecured receivables from foreign brokers are a substantial portion, such as 25 percent, of a firm's assets and, if so, may undertake discussions with the firms concerning the circumstances involved.

[47] *See* 47 FR 18618, 18619 (Apr. 30, 1982).

so, to analyze the economic impact on such entities at that time.[48] The amendments to Rules 1.17(c)(5)(xiii) and (h)(2)(vii) eliminate the capital charge for unsecured receivables from certain foreign brokers and reduce the burden associated with the procedure to obtain approval for prepayment of subordinated debt, respectively. Accordingly, these amendments impose no additional requirements on an independent IB. In addition, the amendment to the minimum adjusted net capital requirement for an IB conforms the Commission's requirement to that of the NFA and therefore there should be no impact on an IB's financial operations. Therefore, these rule amendments will not have a significant economic impact on a substantial number of small entities.

B. Paperwork Reduction Act

The Paperwork Reduction Act of 1980 (PRA), 44 U.S.C. 3501 *et seq.* (1994), imposes certain requirements on federal agencies (including the Commission) in connection with their conducting or sponsoring any collection of information as defined by the PRA. In compliance with the PRA, the Commission submitted the December 1994 proposed rule amendments and their associated information collection requirements to the Office of Management and Budget. The burden associated with that entire collection (3038–0024) including the December 1994 proposed rule amendments, is as follows:

Average Burden Hours Per Response: 18.00.

Number of Respondents: 1,782.

Frequency of Response: annually, quarterly and on occasion.

The burden associated with the December 1994 proposed rule amendments was as follows:

Average Burden Hours Per Response: 1.00.

Number of Respondents: 12.

Frequency of Response: on occasion.

The Office of Management and Budget approved the December 1994 submission concerning collection 3038–0024 on February 1, 1995.

When the Commission proposed rule amendments in December 1995, it noted that the proposed rule amendments had no burden,[49] although Rules 1.12, 1.17 and 1.58 are part of groups of rules with the following burdens.

The burden associated with the collection required by Rules 1.12 and 1.17 (3038–0024), including the rule amendments proposed in December 1995, is as noted above. The burden associated with the collection required by Rule 1.58 (3038–0026), including the rule amendments proposed in December 1995, is as follows:

A. Reporting

Average Burden Hours Per Response: 0.04.

Number of Respondents: 100.00.

Frequency of Response: daily.

B. Recordkeeping

Average Burden Hours Per Response: 1.00.

Number of Respondents: 300.00

Frequency of Response: annually.

Persons wishing to comment on the estimated paperwork burden associated with these rule amendments should contact Jeff Hill, Office of Management and Budget, room 3228, NEOB, Washington, DC 20503 (202) 395–7340. Copies of the information collection submissions to OMB are available from Joe F. Mink, CFTC Clearance Officer, 1155 21st Street, NW., Washington, DC 20581, (202) 418–5170.

List of Subjects in 17 CFR Part 1

Commodity futures, Minimum financial requirements.

In consideration of the foregoing, and pursuant to the authority contained in the Commodity Exchange Act, and in particular Sections 4f(b), 4f(c), 4g and 8a, 7 U.S.C. 6f(b), 6f(c), 6g, and 12a, the Commission hereby amends Part 1 of Chapter I of Title 17 of the Code of Federal Regulations as follows:

PART 1—GENERAL REGULATIONS UNDER THE COMMODITY EXCHANGE ACT

1. The authority citation for Part 1 continues to read as follows:

Authority: 7 U.S.C. 1a, 2, 2a, 4, 4a, 6, 6a, 6b, 6c, 6d, 6e, 6f, 6g, 6h, 6i, 6j, 6k, 6l, 6m, 6n, 6o, 6p, 7, 7a, 7b, 8, 9, 12, 12a, 12c, 13a, 13a–1, 16, 16a, 19, 21, 23 and 24.

2. Section 1.12 is amended by removing the word ''or'' at the end of paragraph (b)(2), by redesignating paragraph (b)(3) as paragraph (b)(4), by adding a new paragraph (b)(3), by adding paragraphs (f)(4) and (f)(5) and by revising the introductory text of paragraph (g), paragraph (g)(1) and paragraph (g)(2) to read as follows:

§ 1.12 Maintenance of minimum financial requirements by futures commission merchants and introducing brokers.

* * * * *

(b) * * *

(3) 150 percent of the amount of adjusted net capital required by a registered futures association of which it is a member; or

* * * * *

(f) * * *

(4) A futures commission merchant shall report immediately whenever any commodity interest account it carries is subject to a margin call, or call for other deposits required by the futures commission merchant, that exceeds the futures commission merchant's excess adjusted net capital, determined in accordance with § 1.17, and such call has not been answered by the close of business on the day following the issuance of the call. This applies to all accounts carried by the futures commission merchant, whether customer, noncustomer, or omnibus, that are subject to margining, including commodity futures and options. In addition to actual margin deposits by an account owner, a futures commission merchant may also take account of favorable market moves in determining whether the margin call is required to be reported under this paragraph.

(f)(5)(i) A futures commission merchant shall report immediately whenever its excess adjusted net capital is less than six percent of the maintenance margin required by the futures commission merchant on all positions held in accounts of a noncustomer other than a noncustomer who is subject to the minimum financial requirements of:

(A) A futures commission merchant, or

(B) The Securities and Exchange Commission for a securities broker and dealer.

(ii) For purposes of paragraph (f)(5)(i), maintenance margin shall include all deposits which the futures commission merchant requires the noncustomer to maintain in order to carry its positions at the futures commission merchant.

(g) A futures commission merchant shall provide written notice of a substantial reduction in capital as compared to that last reported in a financial report filed with the Commission pursuant to § 1.10. This notice shall be provided as follows:

(1) If any event or series of events, including any withdrawal, advance, loan or loss cause, on a net basis, a reduction in net capital (or, if the futures commission merchant is qualified to use the filing option available under § 1.10(h), tentative net capital as defined in the rules of the Securities and Exchange Commission) of 20 percent or more, notice must be provided within two business days of

[48] *See* 48 FR 35248, 35275–78 (Aug. 3, 1983).

[49] The proposed increase in the dollar amount of minimum adjusted net capital for an FCM and IB would necessitate only a change in line item 23E of the Statement of the Computation of Minimum Capital Requirements on Form 1–FR–FCM and in line item 15 of that Statement on Form 1–FR–IB, as well as a calculation of the minimum adjusted net capital requirement based upon a firm's branch offices and APs.

the event or series of events causing the reduction; and

(2) If equity capital of the futures commission merchant or a subsidiary or affiliate of the futures commission merchant consolidated pursuant to § 1.10(f) (or 17 CFR 240.15c3–1e) would be withdrawn by action of a stockholder or a partner or by redemption or repurchase of shares of stock by any of the consolidated entities or through the payment of dividends or any similar distribution, or an unsecured advance or loan would be made to a stockholder, partner, sole proprietor, employee or affiliate, such that the withdrawal, advance or loan would cause, on a net basis, a reduction in excess adjusted net capital (or, if the futures commission merchant is qualified to use the filing option available under § 1.10(h), excess net capital as defined in the rules of the Securities and Exchange Commission) of 30 percent or more, notice must be provided at least two business days prior to the withdrawal, advance or loan that would cause the reduction: *Provided, however,* That the provisions of paragraphs (g)(1) and (g)(2) of this section do not apply to any futures or securities transaction in the ordinary course of business between a futures commission merchant and any affiliate where the futures commission merchant makes payment to or on behalf of such affiliate for such transaction and then receives payment from such affiliate for such transaction within two business days from the date of the transaction.

* * * * *

3. Section 1.17 is amended as follows:

3.1. By revising paragraph (a)(1);

3.2. By revising paragraph (c)(5)(xiii);

3.3. By removing the word ''or'' at the end of paragraph (e)(1)(ii), by redesignating paragraph (e)(1)(iii) as (e)(1)(iv), and by adding a new paragraph (e)(1)(iii);

3.4. By removing the word ''or'' at the end of paragraph (h)(2)(vi)(C)(*2*), by redesignating paragraph (h)(2)(vi)(C)(*3*) as paragraph (h)(2)(vi)(C)(*4*), and by adding a new paragraph (h)(2)(vi)(C)(*3*);

3.5. By removing the word ''or'' at the end of paragraph (h)(2)(vii)(A)(*2*), by redesignating paragraph (h)(2)(vii)(A)(*3*) as paragraph (h)(2)(vii)(A)(*4*) and, as redesignated, revising it, and by adding a new paragraph (h)(2)(vii)(A)(*3*);

3.6. By removing the word ''or'' at the end of paragraph (h)(2)(vii)(B)(*2*), by redesignating paragraph (h)(2)(vii)(B)(*3*) as paragraph (h)(2)(vii)(B)(*4*) and, as redesignated, revising it, and by adding new paragraphs (h)(2)(vii)(B)(*3*) and (h)(2)(vii)(C);

3.7. By removing the word ''or'' at the end of paragraph (h)(2)(viii)(A)(*2*), by redesignating paragraph (h)(2)(viii)(A)(*3*) as paragraph (h)(2)(viii)(A)(*4*), and by adding a new paragraph (h)(2)(viii)(A)(*3*);

3.8. By removing the word ''or'' at the end of paragraph (h)(3)(ii)(B), by redesignating paragraph (h)(3)(ii)(C) as paragraph (h)(3)(ii)(D), and by adding a new paragraph (h)(3)(ii)(C); and

3.9. By redesignating paragraphs (h)(3)(v)(C) and (D) as paragraphs (h)(3)(v)(D) and (E) and by adding a new paragraph (h)(3)(v)(C). The revised and added paragraphs read as follows:

§ 1.17 Minimum financial requirements for futures commission merchants and introducing brokers.

(a)(1)(i) Except as provided in paragraph (a)(2)(i) of this section, each person registered as a futures commission merchant must maintain adjusted net capital equal to or in excess of the greatest of:

(A) $250,000;

(B) Four percent of the following amount: The customer funds required to be segregated pursuant to the Act and these regulations and the foreign futures or foreign options secured amount, less the market value of commodity options purchased by customers on or subject to the rules of a contract market or a foreign board of trade: *Provided, however,* That the deduction for each customer shall be limited to the amount of customer funds in such customer's account(s) and foreign futures and foreign options secured amounts;

(C) The amount of adjusted net capital required by a registered futures association of which it is a member; or

(D) For securities brokers and dealers, the amount of net capital required by Rule 15c3–1(a) of the Securities and Exchange Commission (17 CFR 240.15c3–1(a)).

(ii) Except as provided in paragraph (a)(2) of this section, each person registered as an introducing broker must maintain adjusted net capital equal to or in excess of the greatest of:

(A) $30,000;

(B) The amount of adjusted net capital required by a registered futures association of which it is a member; or

(C) For securities brokers and dealers, the amount of net capital required by Rule 15c3–1(a) of the Securities and Exchange Commission (17 CFR 240.15c3–1(a)).

* * * * *

(c) * * *

(5) * * *

(xiii) Five percent of all unsecured receivables includable under paragraph (c)(2)(ii)(D) of this section used by the applicant or registrant in computing ''net capital'' and which are not receivable from

(A) A registered futures commission merchant, or

(B) A broker or dealer which is registered as such with the Securities and Exchange Commission: *Provided, however,* That if the unsecured receivable represents deposits required to maintain futures and commodity option positions, is receivable from a broker which has been granted comparability relief pursuant to § 30.10 of this chapter, and is held by the broker itself, with another foreign broker that has been granted comparability relief under § 30.10 of this chapter, or at a depository in the same jurisdiction as either foreign broker that would qualify as a depository for funds in accordance with § 30.7 of this chapter, and, in the case of customer funds, is held in accordance with the special requirements of the applicable Commission order issued under § 30.10 of this chapter, there will be no charge.

* * * * *

(e) * * *

(1) * * *

(iii) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member; or

* * * * *

(h) * * *

(2) * * *

(vi) * * *

(C) * * *

(*3*) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member; or

* * * * *

(vii) * * *

(A) * * *

(*3*) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member; or

(*4*) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3–1d(b)(7) of the Securities and Exchange Commission (17 CFR 240.15c3–1d(b)(7)).

(B) * * *

(*3*) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member; or

(*4*) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3–1d(c)(5)(ii) of the Securities and Exchange Commission (17 CFR 240.15c3–1d(c)(5)(ii)): *Provided, however,* That no special prepayment shall be made if pre-tax losses during the latest three-month period were greater than 15 percent of current excess adjusted net capital.

(C) Notwithstanding the provisions of paragraphs (h)(2)(vii)(A) and (h)(2)(vii)(B) of this section, in the case of an applicant, no prepayment or special prepayment shall occur without the prior written approval of the National Futures Association; in the case of a registrant, no prepayment or special prepayment shall occur without the prior written approval of the designated self-regulatory organization, if any, or of the Commission if the registrant is not a member of a self-regulatory organization. The designated self-regulatory organization shall immediately provide the Commission with a copy of any notice of approval issued where the requested prepayment or special prepayment will result in the reduction of the registrant's net capital by 20 percent or more or the registrant's excess adjusted net capital by 30 percent or more.

(viii) * * *

(A) * * *

(*3*) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member; or

* * * * *

(3) * * *

(ii) * * *

(C) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member; or

* * * * *

(v) * * *

(C) 120 percent of the amount of adjusted net capital required by a registered futures association of which it is a member;

* * * * *

4. Section 1.58 is revised to read as follows:

§ 1.58 Gross collection of exchange-set margins.

(a) Each futures commission merchant which carries a commodity futures or commodity option position for another futures commission merchant or for a foreign broker on an omnibus basis must collect, and each futures commission merchant and foreign broker for which an omnibus account is being carried must deposit, initial and maintenance margin on each position reported in accordance with § 17.04 of this chapter at a level no less than that established for customer accounts by the rules of the applicable contract market.

(b) If the futures commission merchant which carries a commodity futures or commodity option position for another futures commission merchant or for a foreign broker on an omnibus basis allows a position to be margined as a spread position or as a hedged position in accordance with the rules of the applicable contract market, the carrying futures commission merchant must obtain and retain a written representation from the futures commission merchant or from the foreign broker for which the omnibus account is being carried that each such position is entitled to be so margined.

Issued in Washington, D.C. on April 25, 1996, by the Commission.

Jean A. Webb,

Secretary of the Commission.

[FR Doc. 96–10714 Filed 4–30–96; 8:45 am]

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DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

Office of the Secretary

24 CFR Part 0

[Docket No. FR–3331–C–02]

RIN 2501–AB55

Reinstatement of Two Sections of HUD's Standards of Conduct Regulation at 24 CFR Part 0; Correction

AGENCY: Office of the Secretary, Department of Housing and Urban Development.

ACTION: Correction to final rule.

SUMMARY: This correction to a final rule issued by the Department of Housing and Urban Development (Department) reinstates two sections of HUD's Standards of Conduct at 24 CFR part 0, that pertain to ''Outside employment and other activities'' and ''Financial interests,'' which were deleted in a final rule published on April 5, 1996.

DATES: Effective Date: May 6, 1996.

FOR FURTHER INFORMATION CONTACT: Aaron Santa Anna, Assistant General Counsel, Ethics Law Division, at (202) 708–3815, or Sam E. Hutchinson, Associate General Counsel, Office of Human Resources Law, (202) 708–0888; 451 Seventh Street, SW., Washington, DC 20410. Hearing or speech-impaired individuals may call HUD's TDD number (202) 708–3259. (Telephone numbers are not toll-free.)

SUPPLEMENTARY INFORMATION: On April 5, 1996, the Department published a final rule that revised the Department's Standards of Conduct regulation at 24 CFR Part 0. This final rule takes effect on May 6, 1996. See 61 FR 15350. The final rule removed 24 CFR part 0 in its entirety and replaced it with a single section that provides a cross reference to the executive branch financial disclosure regulations at 5 CFR part 2634 and the Standards of Ethical Conduct for Employees of the Executive Branch regulation at 5 CFR part 2635 (the Standards). Most of the provisions in 24 CFR part 0 were superseded when 5 CFR parts 2634 and 2635 took effect.

Among the provisions removed from 24 CFR part 0 were two—§ 0.735–203 regarding ''Outside employment and other activities'' and § 0.735–204 regarding ''Financial interests''—that were not superseded by 5 CFR parts 2634 and 2635. Those two provisions remained in effect temporarily under the Notes following 5 CFR 2635.804 and 5 CFR 2635.403(a), as extended at 59 FR 4779–4780, 60 FR 6390–6391, and 60 FR 66857–66858 (see also appendixes A–C to 5 CFR part 2635). The notes are ''grandfather'' provisions that currently preserve until August 7, 1996 (or until issuance of the agency's supplemental standards of ethical conduct regulation, whichever occurs first) such requirements for prior approval of employment or activities, and prohibitions on acquiring or holding a specific financial interest, contained in agency regulations, instructions or other issuances in effect prior to the effective date of the Standards. In accordance with these grandfather provisions, the Department is reinstating removed sections 0.735–203 and 0.735–204 of 24 CFR, renumbered respectively as sections 0.2 and 0.3, to avoid an untimely lapse in enforcement authority pending issuance of the Department's supplemental standards of ethical conduct as a final rule.

On June 30, 1995, the Department published proposed supplemental standards of ethical conduct for its employees. See 60 FR 34420–34426. The proposed rule would establish restrictions on outside employment and activities and prohibitions on the ownership of certain financial interests, similar to those in 24 CFR 0.735–203 and 0.735–204. In that rulemaking document, the Department also proposed to revise 24 CFR part 0 by removing all of the provisions therein and replacing them with a residual provision that would cross reference 5 CFR parts 2634 and 2635, as well as the Department's supplemental standards of ethical conduct to be codified at 5 CFR part 7501. Upon publication of the Department's supplemental standards of ethical conduct as a final rule, the Department will, as proposed at 60 FR 34420–34426, amend the residual cross reference section in 24 CFR part 0 by adding a cross reference to the Department's supplemental standards of ethical conduct at 5 CFR part 7501. In