

COMMODITY FUTURES TRADING COMMISSION**17 CFR Part 1****Minimum Financial Requirements, Prepayment of Subordinated Debt and Gross Collection of Exchange-Set Margin for Omnibus Accounts**

AGENCY: Commodity Futures Trading Commission.

ACTION: Proposed rules.

SUMMARY: The Commodity Futures Trading Commission (Commission) proposes to amend: (1) Rules 1.17(a)(1)(i) and (ii) to (a) increase the minimum required dollar amount of adjusted net capital for futures commission merchants (FCMs) from \$50,000 to \$250,000, (b) increase the minimum required dollar amount of adjusted net capital for introducing brokers (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; (2) Rule 1.17(h)(2)(vii) with respect to the procedure to obtain approval for prepayment of subordinated debt; and (3) 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 industry self-regulatory organizations (SROs) and therefore should not require changes in the operations of most firms.

DATES: Comments on the proposed amendments must be received on or before January 12, 1996.

ADDRESSES: Comments should be sent to Jean A. Webb, Secretary of the Commission, Commodity Futures Trading Commission, 1155 21st Street, NW, Washington, DC 20581. Please refer to "Financial Rule Amendments."

FOR FURTHER INFORMATION CONTACT: Lawrence B. Patent, Associate Chief Counsel, Division of Trading and Markets, Commodity Futures Trading Commission, 1155 21st Street, NW, Washington, DC 20581. Telephone: (202) 418-5439.

SUPPLEMENTARY INFORMATION:**I. Minimum Financial Requirements****A. Minimum Financial Requirements for FCMs**

Rule 1.17(a)(1)(i) requires FCMs to maintain adjusted net capital equal to or

in excess of the greatest of: (1) \$50,000, (2) four percent of the sum of the amount of funds required to be segregated under Section 4d(2) of the Commodity Exchange Act (Act)¹ (i.e., for trading in U.S. markets) and the amount of funds required to be set aside under Commission Rule 30.7² for customers trading foreign markets (referred to as the "secured amount"); or (3) if an FCM is also registered as a securities broker-dealer, the amount of net capital required by the Securities and Exchange Commission (SEC).³ The \$50,000 minimum dollar requirement was established in 1978⁴ and has remained unchanged. On August 27, 1990, the Commission approved amendments to Rule 201 of the Chicago Board of Trade (CBT) and Section 1 of NFA's Financial Requirements increasing their respective FCM members' minimum adjusted net capital requirement to \$250,000.⁵ The NFA proposed the minimum adjusted net capital increase based upon the growth in trading volume in the industry,⁶ the increase in segregated funds per FCM⁷ and the decrease in the value of the dollar that

¹ 7 U.S.C. 6d(2) (1994).

² 17 CFR 30.7 (1995).

³ Commission Rule 170.15 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. National Futures Association (NFA) is the only registered futures association. It has an FCM membership category and virtually all FCMs are NFA members. However, there are approximately 90 firms registered as FCMs (out of a total of approximately 260) that do not handle customer funds and therefore are not required to register as FCMs. Accordingly, these firms are not required to be NFA members pursuant to Commission Rule 170.15 but almost all of them are NFA members anyway. However, there still are approximately ten registered FCMs that are not members of any SRO and thus have a current minimum dollar adjusted net capital requirement of \$100,000 under Commission Rule 1.17(a)(1)(i)(A). Since such a small number of firms are in this category, for ease of discussion we shall assume that all registered FCMs currently have a minimum dollar requirement of adjusted net capital of \$50,000 under Commission rules.

⁴ See 43 FR 39956 (September 8, 1978).

⁵ On November 24, 1992, the SEC also adopted rule amendments to raise its minimum net capital requirement for securities broker-dealers 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).

⁶ This trend has continued. In fiscal year 1990, 334.2 million futures and option contracts were traded on U.S. contract markets, and that number increased more than 50 percent in the last five years to approximately 504.8 million in fiscal year 1995.

⁷ In NFA's 1990 submission, it noted that the average amount of funds in segregation at each FCM more than tripled from 1980 to 1985, increasing from \$8.7 million to \$28.5 million. That amount more than tripled again in the last ten years and now exceeds \$100 million.

had occurred since 1978. The Commission approved these amendments to provide FCM customers with the same degree of protection that was provided by the \$50,000 minimum adjusted net capital requirement when it was originally adopted in 1978.

Pursuant to paragraph (a)(2) of Commission Rule 1.17, the Commission's minimum financial requirements are not applicable to a registrant that is a member of an SRO and that conforms to the minimum financial standards set by such SRO. As noted above, all persons required to register as FCMs are required to be NFA members under Commission Rule 170.15. Consequently, when the Commission approved NFA's amendment of the minimum dollar amount of adjusted net capital required of its member FCMs in 1990, the Commission effectively raised the dollar level of minimum adjusted net capital for all FCMs to \$250,000.

The Commission nonetheless believes that raising the required minimum dollar amount of adjusted net capital for FCMs under Commission Rule 1.17 to that required by NFA and CBT for their members is necessary and appropriate for the following reasons. Section 8c(a)(1) of the Act, 7 U.S.C. 12c(a)(1) (1994), authorizes the Commission to discipline a member of an exchange in accordance with the rules of that exchange if the exchange fails to do so. Section 17(l)(1) of the Act, 7 U.S.C. 21(1)(1) (1994), authorizes the Commission to suspend a registered futures association that has failed to enforce compliance with its own rules. 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. This limitation upon the Commission's enforcement remedies in the context of SRO rules does not, of course, exist in the context of violations of the Act or Commission regulations. Section 6c of the Act, 7 U.S.C. 13a-1 (1994), 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.

The proposed amendment to Rule 1.17(a)(1)(i)(A) thus would permit the Commission to use its authority under Section 6c of the Act to enforce