

worth. In addition, the proposed amendments would provide lower margin requirements for exempt account transactions in investment grade foreign sovereign debt and other investment grade non-equity securities. For transactions in these types of securities, member organizations would be required to take either a net capital charge equal to marked to market losses or collect margin equal to the percentage requirements under the Rule. In this instance, the NYSE believes that the enhanced creditworthiness of both the customer and the security transacted would justify the imposition of lower margin requirements.

Amendment No. 1

In January 1999, the NYSE filed Amendment No. 1 to the Initial Filing. Amendment No. 1 sought to clarify and amend the following with regard to the original filing: (1) Amend NYSE Rule 431(a)(13) to clarify that non-member brokers or dealers that are considered exempt accounts must be registered with the Commission; (2) amend NYSE Rule 431(a)(13) to require that for a person to be considered an exempt account, at least \$45 million of net worth and at least \$40 million of financial assets are required; and (3) amend NYSE Rule 431(e)(2)(H)(i) to require member organizations to maintain written risk analysis procedures for assessing the amount of credit extended to exempt accounts. The NYSE believes that increasing the net worth requirement from \$40 to \$45 million, and including indicia of a person's liquidity (\$40 in financial assets) in that total, provides a better indicator of a person's creditworthiness when extending credit for transactions in non-equity securities in exempt accounts.

In addition, the NYSE states that Amendment No. 1 would require that, as a good business practice and for safety and soundness considerations, member organizations maintain written procedures for assessing credit extended to exempt accounts. Although the requirement for member organizations can be found in interpretations to NYSE Rule 401, "Business Conduct," it is proposed to be codified in NYSE Rule 431.

Information Memo

As noted above, the NYSE has submitted to the Commission a draft Information Memo that it would circulate to its members upon approval of the proposed rule change. The Information Memo would provide guidelines for members to satisfy the requirement to maintain written risk

analysis procedures under proposed NYSE Rule 431(e)(2)(H)(i). Specifically, the Information Memo would provide that a member's written risk methodology for assessing credit extended to exempt accounts should include the following:

- Procedures for obtaining and reviewing the appropriate customer account documentation and the customer financial information necessary to determine exempt account status for the extension of credit under the rule.
- Procedures and guidelines for the determination, review and approval of credit limits to customers and across all customers who qualify as exempt accounts under the rule.
- Procedures and guidelines for monitoring credit risk exposure to the organization relating to exempt account customers.
- Procedures and guidelines for the use of stress testing of exempt accounts in order to monitor market risk exposure from exempt accounts individually and in the aggregate.
- Procedures providing for the regular review and testing of these risk management procedures by an independent unit such as internal audit, risk management, or other comparable group.

Amendment Nos. 2 and 3

In Amendment Nos. 2 and 3, the NYSE proposes to require that persons qualifying for exempt account status satisfy requirements in addition to the net worth and financial assets standards described above. In this regard, the NYSE proposes to require that persons qualifying for exempt account status meet specific registration and reporting requirements under the federal securities laws, specifically the Securities Act of 1933⁷ ("Securities Act") and the Exchange Act, or make available to the member or member organization certain current information regarding the person's ownership, business, operations, and financial condition.

Specifically, in addition to meeting the \$45/\$40 million thresholds, persons qualifying for "exempt account" status also would have to satisfy one of the following requirements: (1) The person must have securities registered pursuant to section 12 of the Exchange Act⁸ and must have been subject to the reporting requirements of section 13 of the Exchange Act;⁹ (2) the person must have securities registered pursuant to

the Securities Act and must have been subject to the reporting requirements of section 15(d) of the Exchange Act;¹⁰ (3) if the person is not subject to section 13 or 15(d) of the Exchange Act, that person must make information available that is required pursuant to Rule 15c2-11 under the Exchange Act;¹¹ or (4) the person must make available to the member organization such current information regarding the person's ownership, business, operations, and financial condition, including such person's audited statement of financial condition, statement of income, and statement of changes in stockholder's equity or comparable financial reports. In addition, a person that meets the financial threshold also could qualify for exempt account status if the person is eligible for an exemption from the Exchange Act reporting requirements because the person furnishes the Commission with information as required under Exchange Act Rule 12g3-2(b).¹²

Sections 13 and 15(d) of the Exchange Act require publicly held companies to furnish to the public on a continuous and ongoing basis certain information regarding their operations and financial condition. Companies subject to this obligation, among others, include: (1) Companies that have registered a class of securities under section 12(b) of the Exchange Act¹³ for listing and trading on a national securities exchange; and (2) an issuer that has filed a registration statement pursuant to the Securities Act that has been declared effective.

Pursuant to Commission rules promulgated under Sections 13 and 15(d) of the Exchange Act, companies are required to make the disclosures noted above on a quarterly (Form 10-Q),¹⁴ annual (Form 10-K),¹⁵ and interim basis (Form 8-K).¹⁶ Requiring persons qualifying for "exempt account" status to meet the disclosure requirements mandated by these sections and rules of the Exchange Act should provide adequate and sufficient information for a member organization to perform a risk analysis of such persons.

Further, Rule 15c2-11 under the Exchange Act precludes a broker-dealer from entering bid or asked quotations in

¹⁰ 15 U.S.C. 78o(d).

¹¹ 17 CFR 240.15c2-11.

¹² 17 CFR 240.12g3-2(b). Amendment No. 3 revises proposed NYSE Rule 431(a)(13)(B)(ii)(4) to clarify that a person seeking exempt account status under that provision must furnish to the Commission the information required by Rule 12g3-2(b) under the Exchange Act.

¹³ 15 U.S.C. 78l(b).

¹⁴ 17 CFR 249.308b.

¹⁵ 17 CFR 249.310b.

¹⁶ 17 CFR 249.308.

⁷ 15 U.S.C. 77a.

⁸ 15 U.S.C. 78l.

⁹ 15 U.S.C. 78m(a).