

implement Section 17(i) of the Exchange Act. These rules are intended, in part, to allow U.S. broker-dealers to compete more effectively in the global securities markets.

- We solicit comment on whether the proposal would promote both efficiency and capital formation.
- We request comment on the competitive benefits to broker-dealers that may result under the proposed rules.
- We also request comment on any anticompetitive effects that may result under the proposed rules.

## VII. Regulatory Flexibility Act Certification

The Commission hereby certifies, pursuant to 5 U.S.C. 605(b), that proposed new Rules 17i-1 through 17i-8, and proposed amendments to Rules 17h-1T, 17h-2T, and 17a-12(l) under the Exchange Act, if adopted, would not have a significant economic impact on a substantial number of small entities.

Proposed new Rules 17i-1 through 17i-8 would create a framework for the Commission to supervise SIBHCs. These rules also would enhance the Commission's supervision of the SIBHC's subsidiary broker-dealers through collection of additional information and examinations of affiliates of those broker-dealers. This framework would include qualification criteria for IBHCs that file Notices of Intention to be supervised by the Commission, as well as recordkeeping and reporting requirements for SIBHCs. An IBHC that meets the criteria set forth in the proposed rules would not be required to become an SIBHC; supervision as an SIBHC is voluntary. Taken as a whole, the proposed framework would permit the Commission to better monitor the financial condition, risk management, and activities of a broker-dealer's parent and affiliates on a group-wide basis. In particular, it would create a formal process through which the Commission could access important information regarding activities of a broker-dealer's affiliates that could impair the financial and operational stability of the broker-dealer or the SIBHC. Further, as this framework for oversight is voluntary, we do not believe IBHCs will file Notices of Intention to be supervised by the Commission as SIBHCs unless the benefits of such supervision outweigh the costs with respect to the applying firm. The Commission is also proposing to add an exemption to the risk

assessment rules to exempt a broker-dealer that is affiliated with an SIBHC because the SIBHC will be maintaining records and reporting to the Commission regarding the financial and operational condition of members of the affiliate group. Finally, the Commission is proposing to adjust the audit requirements for OTC derivative dealers to allow accountants to use agreed-upon procedures when conducting audits of risk management control systems.

An IBHC can apply to become an SIBHC only if it is not affiliated with an insured bank (with certain exceptions) or a savings association,<sup>157</sup> (ii) a foreign bank, foreign company, or a company that is described in section 8(a) of the International Banking Act of 1978, or (iii) a foreign bank that controls a corporation chartered under section 25A of the Federal Reserve Act.<sup>158</sup> In addition, pursuant to paragraph (d)(2)(i)(B) of proposed Rule 17i-2, the Commission would not consider such supervision necessary or appropriate unless the investment bank holding company demonstrates that it owns or controls a broker or dealer that has a substantial presence in the securities business, which may be demonstrated by a showing that the broker or dealer maintains tentative net capital of \$100 million or more. Accordingly, an IBHC could not be a small entity.<sup>159</sup>

The proposed changes to Rules 17h-1T and 17h-2T would apply only to broker-dealers that are affiliated with an IBHC that becomes supervised by the Commission as an SIBHC. In addition, Rules 17h-1T and 17h-2T only require that one broker-dealer within a holding company structure obtain and maintain the required records and file the required reports. Generally, a broker-dealer would be exempt from Rules 17h-1T and 17h-2T if it (i) maintains less than \$250,000 in net capital, (ii) is exempt from Rule 15c3-3 pursuant to § 240.15c3-3(k)(1), (iii) maintains less than \$20 million in net capital and is either exempt from Rule 15c3-3 pursuant to § 240.15c3-3(k)(2) or is not exempt from Rule 15c3-3 but does not hold funds or securities for, nor owe money or securities to customers. Thus, no small broker-dealers are subject to Rules 17h-1T and 17h-2T.

Rule 17a-12 is only applicable to OTC derivatives dealers. As stated previously, a broker-dealer generally would be considered a small entity if (i) it has total capital (net worth plus subordinated liabilities) of less than \$500,000 on the date in the prior fiscal

year as of which its audited financial statements were prepared pursuant to Rule 17a-5(d) or, if not required to file such statements, a broker-dealer that had total capital (net worth plus subordinated liabilities) of less than \$500,000 on the last day of the preceding fiscal year (or in the time that it has been in business, if shorter); and (ii) it is not affiliated with any person (other than a natural person) that is not a small business or small organization.<sup>160</sup> An OTC derivatives dealer is a "dealer" under the Exchange Act.<sup>161</sup> The minimum capital requirements for an OTC derivatives dealer are tentative net capital of at least \$100 million and net capital of at least \$20 million. Thus, no small broker-dealers are subject to Rule 17a-12.

Accordingly, proposed new Rules 17i-1 through 17i-8, and the proposed amendments to Rules 17h-1T, 17h-2T, and 17a-12(l), if adopted, would not have a significant economic impact on a substantial number of small entities.

We encourage written comments regarding this certification. We solicit comment as to whether the proposed rules and rule amendments could have an effect that we have not considered. We request that commenter describe the nature of any effect on small entities and provide empirical data to support the extent of the effect.

## VIII. Consideration of Impact on the Economy

For purposes of the Small Business Regulatory Enforcement Fairness Act of 1996, or "SBREFA,"<sup>162</sup> we must advise OMB as to whether the proposed regulation constitutes a "major" rule. Under SBREFA, a rule is considered "major" where, if adopted, it results or is likely to result in:

- An annual effect on the economy of \$100 million or more (either in the form of an increase or a decrease);
- A major increase in costs or prices for consumers or individual industries;
- or
- Significant adverse effect on competition, investment or innovation.

If a rule is "major," its effectiveness will generally be delayed for 60 days pending Congressional review. We request comment on the potential impact of the proposed regulation on the economy on an annual basis. Commenters are requested to provide empirical data and other factual support for their view to the extent possible.

<sup>160</sup> Exchange Act Rule 0-10 [17 CFR 240.0-10].

<sup>161</sup> See Section 3(a)(5) of the Exchange Act [15 U.S.C. 78c(a)(5)].

<sup>162</sup> Pub. L. No. 104-121, Title II, 110 Stat. 857 (1996) (codified in various sections of 5 U.S.C., 15 U.S.C., and as a note to 5 U.S.C. 601).

engage in international transactions that could cause them to be subject to regulation by international securities regulatory agencies.

<sup>157</sup> See *supra*, note 6.

<sup>158</sup> Federal Reserve Act § 25A [12 U.S.C. 611].

<sup>159</sup> See 17 CFR 240.0-10(c).