

a broker or dealer that are reasonably likely to have a material impact on the financial and operational condition of the broker or dealer. Proposed Rule 17h-2T would require registered broker-dealers to file with the Commission quarterly summary reports of the information required to be maintained and preserved by Rule 17h-1T. The temporary rules are being proposed pursuant to the authority conferred on the Commission by the risk assessment provisions of the Market Reform Act of 1990 and are intended to give the Commission access to information concerning the financial and securities activities of certain broker-dealer affiliates. The Commission requests comment on the proposed rules. In particular, the Commission requests comment on whether, and to what extent, reports or information filed by associated persons of broker-dealers with other domestic or foreign regulatory entities would be sufficient for Commission risk assessment purposes.

DATES: Comments to be received on or before November 5, 1991.

ADDRESSES: Persons wishing to submit written comments should file three copies with Jonathan G. Katz, Secretary, Securities and Exchange Commission, 450 Fifth Street NW., Stop 6-9, Washington, DC 20549. All comment letters should refer to File No. S7-25-91. All comments received will be available for public inspection and copying in the Commission's Public Reference Room, 450 Fifth Street NW., Washington, DC, 20549.

FOR FURTHER INFORMATION CONTACT: Michael A. Macchiaroli, (202) 272-2904 or Roger G. Coffin, (202) 272-2396, Division of Market Regulation, 450 Fifth Street NW., Washington, DC 20549.

SUPPLEMENTARY INFORMATION:

I. Introduction

A. Background

During the past decade, the securities markets have experienced expansion and evolution. The volume of trading on the securities exchanges and in the over-the-counter markets has grown tremendously. The development of innovative financial products, such as stock index futures, has linked the securities and commodities futures markets through complex trading strategies implemented by major market participants. Advances in communications and information technology have accelerated the pace at which information is disseminated through the markets, increasing the speed at which the markets react to

information. Trading has expanded beyond national borders; a global marketplace has unfolded.

Market participants have adapted and transformed along with the markets. Where formerly participants in the U.S. securities markets were primarily individual investors, today's markets are often dominated by institutional investors. The broker-dealer community has reacted to the changes in the financial landscape through expansion and diversification. Many broker-dealers have begun to rely less on traditional revenue sources, such as agency transactions, and have become involved in activities such as proprietary trading and merchant banking, which require large capital bases. To acquire the capital necessary to remain competitive in a rapidly expanding global marketplace, firms have turned to the public equity markets, have increased their leverage, or have merged or affiliated themselves with other entities.

As a consequence, many large investment banking firms are now owned by holding companies that have other subsidiaries engaging in financial and securities related activities throughout the globe. In many instances, the holding companies or affiliates of the broker-dealer operate with little or no regulatory oversight. These unregulated entities can attain a degree of leverage and assume credit risks which registered broker-dealers, subject to the Commission's net capital and customer protection rules, cannot. Specifically, many potentially risky activities, such as interest rate swaps, bridge loans, and foreign currency transactions are affected by unregulated holding companies and affiliates of the broker-dealer.¹ In some cases, the registered broker-dealer's parent or affiliates have significantly less capital than the broker-dealer. Where this occurs, creditors may rely on the credit standing of the broker-dealer and the ability of the holding company to obtain capital from the broker-dealer to support bridge financing or other extensions of credit.

¹ The Staff of the Commission, based on conversations with investment banking representatives and financial experts, has estimated that some of the affiliate entities of the major broker-dealers have outstanding, at any given point in time, \$50 billion to \$100 billion in interest rate swaps (based on the notional amount of those transactions) and \$15 billion in foreign currency transactions. In addition, the Staff estimates that the holding companies of the ten largest firms have outstanding approximately \$2 billion in bridge loans.

17 CFR Parts 240 and 249

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Proposed Temporary Risk Assessment Rules

AGENCY: Securities and Exchange Commission.

ACTION: Proposal of Temporary Rules 17h-1T and 17h-2T.

SUMMARY: The Securities and Exchange Commission is proposing for comment temporary Rules 17h-1T and 17h-2T (17 CFR 240.17h-1T and 17 CFR 240.17h-2T) under the Securities Exchange Act of 1934 (the "Exchange Act"). Proposed Rule 17h-1T would require broker-dealers to maintain and preserve records and other information concerning certain of the broker-dealer's associated persons. The requirement to maintain and preserve records and other information under proposed Rule 17h-1T would extend to the financial and securities activities of the holding companies, affiliates, or subsidiaries of

B. Existing Regulatory Framework

Existing Commission regulations deal with capital requirements designed to insulate broker-dealers and their customers from the business failure of the regulated broker-dealer. Specifically, the net capital rule requires that capital sufficient to meet reasonable anticipated business and trading losses remain in the broker-dealer at all times. Moreover, the customer protection rule ensures that customers' fully paid and excess margin securities are segregated and imposes strict controls on use of other customer funds and securities.

Rule 15c3-1 under the Exchange Act (17 CFR 240.15c3-1), the Commission's net capital rule, protects customers and creditors of registered broker-dealers from monetary losses and delays that can occur when the registered broker-dealer fails. In this way, the net capital rule acts to prevent systemic risk from the failure of a financial intermediary. The net capital rule requires registered broker-dealers to maintain sufficient liquid assets to enable firms that fall below the minimum capital requirements to liquidate in an orderly fashion without a formal proceeding. By concentrating on the financial condition of the broker-dealer, the net capital rule insulates the broker-dealer and its customers from financial failures or difficulties of affiliated entities.²

Rule 15c3-3 under the Exchange Act (17 CFR 240.15c3-3), the customer protection rule, complements the net capital rule by preventing the misallocation or misuse of customer funds or securities by broker-dealers. Among other things, the customer protection rule limits a broker-dealer's use of customer monies to finance the broker-dealer's businesses, except as necessary to finance customer transactions. Both the customer protection and the net capital rules focus specifically on the broker-dealer

itself; the financial condition or the activities of holding companies, affiliates, or subsidiaries are not taken into account. Other recordkeeping and reporting rules enable the Commission to obtain records relating to the financial viability of the registered broker-dealer. Rule 17a-5 under the Exchange Act, 17 CFR 240.17a-5, requires registered broker-dealers to file with the Commission and the broker-dealer's designated examining authority various reports concerning the financial and operational condition of the broker-dealer.³

Rules 17a-3 and 17a-4 under the Exchange Act (17 CFR 240.17a-3 and 17 CFR 240.17a-4), provide for record maintenance and preservation. Rule 17a-3 specifies which records broker-dealers must preserve and maintain. Rule 17a-4 specifies, among other things, that the records and other information required to be kept pursuant to Rule 17a-3 must be maintained in a readily accessible place. Rule 17a-4 also specifies the time periods that broker-dealers must preserve the records required by it and by Rule 17a-3.

Overall, the Commission's financial responsibility and reporting rules have successfully provided a regulatory framework for the protection of customers and creditors of registered broker-dealers. However, while these rules call for detailed financial and operational information of the registered broker-dealer, they do not require the broker-dealer to maintain and preserve records with respect to the activities of its holding company or affiliated parties. Although the rules provide a sound regulatory structure, they do not completely shelter the broker-dealer from the failures of affiliated entities. Broker-dealers are affected by the financial difficulties of affiliated entities both directly, by the withdrawal of capital to meet the obligations of affiliates, and indirectly, by the effect such difficulties can have on the broker-dealers' ability to obtain financing.

This impact on a broker-dealer can be exacerbated in times of market stress. Access to information concerning the activities of associated persons of broker-dealers is particularly pertinent during periods of steep market decline and volatility. For instance, the Commission was particularly concerned about the liquidity and funding of broker-dealers during both the October 1987 market break and the market turbulence of October 1989. Those incidents demonstrated that plunging

stock prices may generate an environment of uncertainty that will impact the financial operation of broker-dealers. An abrupt decline in the market can increase the credit risk involved in lending to broker-dealers holding large inventories of equity relative to their capital, lenders may thus become reluctant to continue extending credit. In addition, some broker-dealers may experience temporary difficulties in marketing instruments the proceeds of which are needed to satisfy the financial obligations (e.g., bridge loans) of their clients. Events such as these could lead to a funding or liquidity problem for the holding company parent of a broker-dealer, which may be forced to look to the net capital of the broker-dealer as a means of funding the parent's business.

Likewise, regulatory concerns about the financial condition of broker-dealers can arise at times other than periods of market decline. For example, the activities carried out by the affiliates of a broker-dealer are, in the aggregate, generally more highly leveraged and riskier than permitted by the net capital rule. If a highly leveraged holding company or other affiliate encounters financial difficulties, its financial distress may extend to the registered firm. Financial problems at the holding company level or in a significant affiliate or subsidiary could impact the ability of the broker-dealer to obtain short-term financing to meet its operating and settlement obligations.

Short-term financings, particularly through the commercial paper market and repurchase agreements, are common financing devices for broker-dealers. If the holding company complex faced a financial predicament, a creditor or contra party might force the broker-dealer to provide additional securities as margin for its repurchase agreements. Even a small increase in required margin levels could force the broker-dealer to liquidate its repurchase agreements and might drastically reduce the firm's short-term financing ability. Similarly, banks may withdraw lines of credit or restrict lending arrangements with broker-dealers because the fiscal health of a related entity has deteriorated. Accordingly, the ability of a broker-dealer to continue operations if a major affiliate ceased operations or met with financial difficulties could be severely impaired. Furthermore, the abrupt liquidation of transactions by a large broker-dealer could seriously affect other market participants as well as disturb the markets themselves.

These concerns are illustrated by the bankruptcy of Drexel Burnham Lambert Group, Inc. ("Drexel"), the holding

² However, the fate of a broker-dealer may be inextricably linked to that of its affiliates. Recently, the Commission adopted amendments to the net capital rule concerning the withdrawal of capital from a broker-dealer by a parent or an affiliate. See Securities Exchange Act Release No. 28927 (February 28, 1991); 56 FR 9124, (March 5, 1991). The amendments require broker-dealers to notify the Commission of large capital withdrawals made to benefit affiliates, subsidiaries and other persons related to the broker-dealer. The amendments also prohibit withdrawals of capital if the withdrawals would cause the broker-dealer's net capital to be less than 25 percent of the deductions required by the net capital rule as to the broker-dealer's readily marketable securities. Finally, the amendments give the Commission the authority to halt, by order, certain withdrawals of capital on a temporary basis in emergency situations. The amendments reflect the Commission's growing concern about the effect that related entities can have on the viability of a broker-dealer.

³ These reports are filed on the Financial and Operational Combined Uniform Single Report (commonly known as the FOCUS report).

company parent of Drexel Burnham Lambert, Inc. ("DBL"), a registered broker-dealer. In this case, Drexel had over \$1 billion in commercial paper and other unsecured short-term borrowings outstanding. As a result of significant losses and a downgrade in the rating of its commercial paper, Drexel found it increasingly difficult to renew its short-term borrowings. Drexel was then forced to turn to the only liquid sources of capital in its assets—the excess net capital of DBL and that of an affiliated government securities dealer.

In a period of approximately three weeks, and without the knowledge of the Commission or the New York Stock Exchange, Inc. ("NYSE"), approximately \$220 million of the excess capital was transferred from the broker-dealer to the holding company in the form of short-term loans. When the Commission became aware of the situation, Drexel or its affiliates had more than \$400 million in short-term liabilities maturing in two weeks and an additional \$330 million maturing the next month.

Ultimately, the Commission and the NYSE intervened and prohibited further withdrawals of capital from the registered broker-dealer. Nonetheless, after the bankruptcy filing by its parent Drexel, DBL was forced to declare bankruptcy and liquidate its assets. This case clearly demonstrated that the viability and the ultimate survival of a broker-dealer can be linked to that of its associated persons.⁴

C. The Market Reform Act

Recently, Congress passed the Market Reform Act of 1990 (the "Reform Act") in response to these and other factors.⁵ The Reform Act is designed to strengthen the system of regulatory oversight over the securities markets and improve the Commission's regulatory supervision over broker-dealers. Section 4 of the Reform Act entitled "Risk Assessment for Holding Company Systems" added section 17(h) of the Exchange Act.⁶

Section 17(h) provides the Commission with specific authority to obtain information regarding certain activities of broker-dealer affiliates, but does not provide the Commission with any new authority to regulate the

activities of those affiliates. New Section 17(h) augments the Commission's broad authority with respect to matters relating to the financial responsibility of broker-dealers and builds on the Commission's statutory authority to adopt recordkeeping and reporting requirements for broker-dealers under section 17(a) of the Exchange Act.

Section 17(b) requires broker-dealers to maintain and preserve such risk assessment information as the Commission by rule prescribes with respect to those associated persons of the broker-dealer whose "business activities are reasonably likely to have a material impact on the financial and operational condition" of the broker-dealer, including the broker-dealer's "net capital, its liquidity, or its ability to finance its operations".⁷ The statute provides that the records should concern the broker-dealer's "policies, procedures, or systems for monitoring and controlling financial and operational risks to it resulting from the activities" of its material associated persons and should "describe, in the aggregate, each of the financial and securities activities conducted by, and the customary sources of capital and funding" of associated persons whose business activities are reasonably likely to have a material impact on the broker-dealer.⁸ In addition, the Reform Act authorizes the Commission to require broker-dealers to file, no more frequently than quarterly, summary reports of the information and records maintained pursuant to the risk assessment rules.⁹

The Reform Act does not contain a definition of the term "financial and securities activities"; however, the legislative history of the bill illustrates the types of activities that are intended to be included in this term.¹⁰ The list encompasses activities generally understood to be engaged in by entities active in the financial markets. However, several activities, such as manufacturing, consumer lending and certain insurance activities are excluded and are beyond the scope of the risk assessment rules.

Section 17(h) of the Act also empowers the Commission to obtain more detailed reports (sometimes referred to as "call reports") during periods of market stress or when information contained in the quarterly reports or other information leads the

Commission to conclude that supplemental information is necessary.

The risk assessment provisions provide the Commission with broad authority, either by rule or by order, to exempt persons or classes of persons from the recordkeeping or reporting requirements. The Commission may grant conditional, permanent or temporary exemptions. The statute directs the Commission to consider a number of factors in granting exemptions which are discussed in greater detail below.

The statute provides that, notwithstanding any other provision of law, the Commission may not be compelled to disclose any information required to be reported by a broker-dealer pursuant to the risk assessment rules or supplied to the Commission by any domestic or foreign regulatory agency.¹¹ The statute expressly exempts risk assessment information from disclosure to the public under the Freedom of Information Act. However, the Commission is not authorized by the statute to withhold risk assessment information from Congress, or from complying with a request for information from any other Federal agency or department requesting the information for purposes within the scope of such agency or department's jurisdiction, or from complying with an order of a court of the United States in an action brought by the United States or the Commission.

II. Proposed Risk Assessment Rules

The Commission preliminarily believes it would be appropriate to propose for public comment two temporary risk assessment rules. The first is a recordkeeping rule which would describe the records and other information that broker-dealers would be required to preserve and maintain. The provisions of proposed Rule 17h-1T apply to all registered broker-dealers and to all municipal securities dealers for which the Commission is the appropriate regulatory agency.

The second would be a reporting rule, and together with the proposed Form 17-H, would set forth the reporting requirements for broker-dealers. Under proposed Rule 17h-2T, broker-dealers would be required to file quarterly reports summarizing the information, records, and any other material compiled pursuant to proposed Rule 17h-1T. Rules 17h-1T and 17h-2T are being proposed on a temporary basis to initiate the risk assessment program as soon as practicable. The Commission

⁴ The Commission believes that the amendments regarding capital withdrawals will enable it to monitor diversions of capital within a multi-layered holding company structure and to anticipate and respond to similar scenarios. For a more detailed description of the Drexel scenario, see Securities Exchange Act Release No. 28347, (August 15, 1990); 55 FR 34027, (August 21, 1990).

⁵ Pub. L. No. 101-432, 104 Stat. 963 (1990). The Reform Act also addresses other changes in the nation's securities markets.

⁶ 15 U.S.C. §9q(h).

⁷ See section 17(h)(1) of the Act.

⁸ *Id.*

⁹ *Id.*

¹⁰ See H.R. Rep. No. 3657, 101st Cong., 2d Sess., at 34 (1990) (hereinafter the "H. Rep.").

¹¹ See section 17(h)(5) of the Act.

expects that final rules will be proposed and adopted after the staff has gained some experience with the information obtained pursuant to the temporary rules.

A. Reporting and Recordkeeping Requirements

Proposed Rule 17h-1T would require broker-dealers to maintain and preserve two general categories of information concerning each Material Associated Person of the broker-dealer.¹² The first concerns the holding company organization and risk management policies. The second concerns the financial condition of the enterprise and includes information such as consolidating and consolidated financial statements. The records and information required to be maintained and preserved pursuant to proposed Rule 17h-1T will be subject to routine inspection by the Commission. Pursuant to proposed Rule 17h-2T, the reporting rule, broker-dealers will be required to file quarterly summaries of the information maintained pursuant to Rule 17h-1T on proposed Form 17-H. The following general categories of information will be required.

1. Organization, Policies and Risk Management Procedures

(a) *Organizational Chart.* Paragraph (a)(1)(i) of proposed Rule 17h-1T would require a broker-dealer to maintain an organizational chart of the holding company structure. This chart should provide a bird's eye view of the entire organization. Included in the organizational chart would be a designation of which associated persons are Material Associated Persons, together with a statement of the major business lines conducted by the associated persons. The organizational chart would also reflect a flow chart of the organization's consolidation process, which the Commission understands is normally prepared as a part of the audit procedure. Proposed Form 17-H specifies that the chart would be included in the first risk assessment filing made by the broker-dealer and in the year end filing. Quarterly updates are required only when a significant change has occurred in the information on file with the Commission.

¹² The term "Material Associated Person" is defined in the proposed rules. The recordkeeping and reporting requirements of the proposed risk assessment rules would only extend to those associated persons designated as "Material Associated Persons" by the broker-dealer. The guidelines to be used by broker-dealers in designating Material Associated Persons are discussed in Part B of this section, *infra*.

(b) *Risk Management Policies.* Paragraphs (a)(1)(ii) through (iv) of proposed Rule 17h-1T would require broker-dealers to maintain specific types of risk management policies. The records required will relate to the broker-dealer's procedures or standards for monitoring and controlling the risks to it resulting from the activities of the Material Associated Persons and would include policies regarding the broker-dealer's and each Material Associated Person's: (1) Credit controls and collateral procedures; (2) sources of funding; and (3) trading risks. The types of policies and procedures required by the risk assessment rules would pertain to the financial and securities activities of the Material Associated Persons only insofar as such activities relate to, or could have an impact on, the registered broker-dealer. The Commission believes these records will be instrumental in attaining an understanding of the internal risk management arrangements in place in the industry. Broker-dealers would be required to include copies of these policies in the first Form 17-H filing and update them on a quarterly basis only if a material change has occurred in the information on file with the Commission.

(c) *Material Legal Proceedings.* Paragraph (a)(1)(v) would require broker-dealers to keep records that describe all material pending legal or arbitration proceedings that are required to be disclosed under generally accepted accounting principles to which any Material Associated Person is a party, or of which any of its property is the subject. This information should be kept in generally the same form and content required by Item 103 of Regulation S-K. This information would be filed with the Commission in the broker-dealer's first Form 17-H; updates would be required only where a material change in the information on file with the Commission has occurred.

(d) *Capital Adequacy Information.* Paragraph (a)(1)(vi) would require broker-dealers to maintain capital adequacy information concerning each Material Associated Person. This item would require records to be maintained concerning: (1) Information relating to total equity and regulatory capital relative to assets; (2) a brief narrative discussion by management concerning the liquidity of assets; and (3) information about the sources of and plans for raising outside capital. Broker-dealers would be required to file these policies with the Commission on an annual basis.

The Commission preliminarily believes that many broker-dealers and

their affiliates generally create the records embodying the types of policies, procedures, and standards required by the risk assessment rules for rating agency, internal or other uses. Moreover, the Commission wishes, wherever possible, to allow broker-dealers to use information that is publicly available or has been created for other use. Therefore, the Commission requests comment on the potential impact of these requirements as well as on what types of records are regularly maintained by broker-dealers for internal risk management purposes.

2. Financial Information

As noted above, the second general category of risk assessment information required by proposed Rule 17h-1T includes financial information pertinent to assessing risk in the holding company system. A quarterly summary of the majority of this information will be required to be filed pursuant to proposed Rule 17h-2T.

(a) *Financial Statements.*—The Commission believes that the information contained in the financial statements will be one of the most important elements of the risk assessment filing with the Commission. The following financial statements, on a consolidating and consolidated basis, would be required: (1) Balance sheet; (2) statement of income; (3) statement of cash flows; and (5) notes to the financial statements. The consolidating and consolidated financial statements should include the broker-dealer's ultimate parent and all of its associated entities and depict the organization on a total entity basis to enable the staff to assess its overall financial condition.¹³

The financial statements would be required to be prepared in the form and content specified by Regulation S-X and would be prepared in accordance with generally accepted accounting principles in the United States ("U.S. GAAP"). With respect to associated persons that use a comprehensive set of accounting principles other than U.S. GAAP, a reconciliation to U.S. GAAP should be included in a note to the financial statements. The note should indicate the comprehensive body of accounting principles used to prepare the financial statements. The reconciliation of U.S. GAAP may, however, be limited to income from continuing operations before income taxes and the equity portion of the balance sheet. The

¹³ In case where it would be appropriate, a broker-dealer could combine into a single entry a number of immaterial entities that do not have significant operating revenues.

reconciliation should provide a narrative description of the items that are treated differently by U.S. GAAP and should quantify such items if the Material Associated Person is required to prepare a quantitative comparison to U.S. GAAP under any applicable federal law.

The financial statements should also be accompanied by the footnotes required by GAAP and any other information necessary for an understanding of the information being presented (e.g., summary of significant accounting policies). However, the Commission believes that the additional footnotes required by Regulation S-X but not required by GAAP may be omitted.

Additionally, the notes to the financial statements required by GAAP should be provided only for the consolidated financial information. Footnote disclosure which would substantially duplicate the disclosure contained in the most recent annual consolidated financial statements may be omitted from the quarterly financial statements.

The quarterly financial statements should include information on both a quarterly and year-to-date basis. Comparative financial statements should also be filed for the quarterly and year-to-date consolidated financial information. For further instructions, broker-dealers should refer to Form 17-H which contains a comprehensive set of instructions to be used by broker-dealers in completing the financial statement requirement.

(b) *Aggregate Securities and Commodities Positions.* Aggregate securities and commodities information will be critical to understanding the investment and trading activities of each Material Associated Person and will permit the staff to evaluate the degree of risk undertaken by each firm. Paragraph (a)(2)(iii) would include the aggregate amount of limited partnership interests owned by each Material Associated Person. Aggregate position data, in a level of detail roughly comparable to that required by the FOCUS reports, will be required to be filed quarterly on Form 17-H. Additionally, the rules require a separate listing of each position where any single position exceeds a defined Materiality Threshold.¹⁴

¹⁴ The term "Materiality Threshold" is defined in the proposed rules to mean the greater of: (A) \$100 million; or (B) 10 percent of the broker-dealer's tentative net capital or 10 percent of the Material Associated Person's tangible net worth, whichever is greater.

The Commission requests comment on the burdens imposed by a requirement to compile aggregate position data. In particular, commentators should address whether this information is currently maintained, and whether it can be compiled within the time frames established by the proposed risk assessment rules. The Commission also requests comment on the impact the aggregate securities and commodities requirement could have on any "Chinese Wall" protections put in place by broker-dealers to alleviate insider trading concerns.

(c) *Aggregate Amounts of Interest Rate Swaps and Other Financial Instruments With Off-Balance Sheet Risk.* Paragraph (a)(2)(iv) of proposed Rule 17h-1T would require broker-dealers to maintain records which reflect the aggregate notional amounts and gross payments owed under interest rate swaps, currency exchange swaps, forward agreements, commodity or stock index swaps or other financial instruments with off-balance sheet risk where the Material Associated Person incurs principal risk or otherwise operates a trading book. For the purposes of this requirement, the term "financial instruments with off-balance sheet risk" has the meaning given in Statement of Financial Accounting Standards No. 105. However, only trading commitments would fall within the scope of this requirement. Commitments made in connection with non-financial or non-securities activities, such as where a Material Associated Person enters into a currency exchange agreement to minimize currency risk in long-term contract with an overseas entity would not be reported. Aggregate quarterly summaries of this information would be filed on Form 17-H, with a separate entry of each commitment where the notional or contractual amount exceeds the Materiality Threshold.

(d) *Bridge Loans and Material Unsecured Extensions of Credit.* Historically, bridge loans have been among the riskier activities conducted by the associated persons of brokerage houses. Although the Commission understands that the amount of new bridge loan financing has declined significantly or has ceased altogether and is not currently a major problem, current exposures need to be monitored on an ongoing basis. Aggregate data would be maintained and filed with the Commission, with a separate listing of large exposures.

(e) *Material Credit Extensions Between a Material Associated Person and Other Associated Persons Whether*

or Not Designated Material Associated Persons. Paragraph (a)(2)(vi) would cover a material loan by a Material Associated Person to an affiliate outside of the immediate or secondary holding company structure which may not be designated a Material Associated Person. The Commission believes this information will help to provide an early warning function in situations where sudden capital distributions presage funding or other financial difficulties in the holding company system.

(f) *Commercial Paper and Other Financing Information.* Many broker-dealers rely on short-term financing, chiefly commercial paper, to fund their daily operations. Most of the commercial paper is issued by the immediate holding company of the registered broker-dealer, and the Commission believes that careful monitoring of this important funding source will be an integral component of the risk assessment program. Paragraph (a)(2)(vii) of proposed Rule 17h-1T would require information regarding any financing arrangement where a payment is scheduled to be made by a Material Associated Person within one year.

(g) *Investments in Affiliated Companies.* Paragraph (a)(2)(viii) of proposed Rule 17h-1T would require broker-dealers to keep records concerning each Material Associated Person's investments in associated companies. This item will be useful, in conjunction with the financial statements, to analyze the overall financial structure of the reporting entities.

(h) *Material Mortgage Loan and Real Estate Activities.* The Commission is particularly concerned about the impact mortgage loans and real estate investments made by Material Associated Persons could have on the broker-dealer. Therefore, the Commission expects the staff to pay particular attention to these activities.

Included in the recordkeeping and reporting requirements would be information regarding the real estate or mortgage loan or investment type (e.g., commercial or residential), a geographic distribution and breakdown of such activities by year, and information about non-performing and defaulting investments or loans. The Commission stresses that here, as well as throughout the risk assessment recordkeeping and reporting rules, broker-dealers are encouraged to utilize data that has been already created for regulatory or internal management use. Moreover, the Commission solicits comment on the types of records created for management and whether the proposed

rules will create a significant recordkeeping and reporting burden.

(i) *Material Lease Financing Activities.* Aggregate data concerning the lease financings activities of Material Associated Persons will be required. Certain broker-dealer affiliates currently engage in activities consisting of direct financing and leveraged leasing of transportation, data processing and other equipment and facilities. Quarterly data would be filed to the Commission on Form 17-H.

The Commission requests comment on the above recordkeeping and reporting requirements. Specifically, the Commission requests comment from broker-dealers that are owned by foreign entities or other U.S. regulated companies that currently file financial information with such foreign or U.S. regulatory agencies. The exemptive provisions of Rules 17h-1T and 17h-2T permit the Commission to accept, in appropriate circumstances, the financial statements and other data filed with other regulatory bodies for the purposes of risk assessment. The Commission therefore requests comment on the form and content of such financial data and whether, and in what circumstances it would be appropriate to allow broker-dealers to file, without reformatting, already existing financial information with the Commission.

B. Scope of Risk Assessment Rules

The statutory standard requires broker-dealers to keep records with respect to those associated persons of the broker-dealer whose "business activities are reasonably likely to have a material impact on the financial and operational condition of the broker-dealer". The term associated person of a broker or dealer is defined in section 3(a)(18) of the Exchange Act.¹⁵ For the purposes of the risk assessment rules, the term does not include natural persons.¹⁶

The Reform Act does not define which associated persons would fall under the statutory standard; however, the legislative history accompanying the Reform Act suggests a flexible facts and circumstances approach.¹⁷ The

determination of which associated persons are material to the registered broker-dealer should depend on an examination of the relevant facts and circumstances. In this regard, the Commission does not believe it would be appropriate to establish a rigid test that would apply to all associated persons in all circumstances because of the many diverse holding company structures that currently own all or a part of registered broker-dealer. Rather, the Commission preliminarily believes that it would be appropriate, especially in the initial phase of the risk assessment program, to leave the determination of which affiliates would have a material impact up to the reporting broker-dealer. Therefore, the proposed rules include the concept of a "Material Associated Person," the designation of which would trigger the risk assessment recordkeeping and reporting obligations.

In determining whether an associated person is a Material Associated Person, however, broker-dealers must generally consider the nature of the legal and financial relationship between the broker-dealer and its associated person, the probability that the associated person's activities may have an adverse impact on the firm, and the magnitude of that impact. Proposed Rule 17h-1T includes an illustrative list of factors relevant to a materiality determination. The following factors are contained in the proposed rule.

The first relevant factor to the determination of materiality is the nature and proximity of the relationship between the registered firm and an associated person. The relationship may depend on the position a broker-dealer occupies within a holding company hierarchy. For example, some broker-dealer holding company structures consist of at least two layers. The first holding company level usually includes the direct holding company parent of the broker-dealer and a number of related financial services entities. The Commission preliminarily believes the activities of these entities are unquestionably material to the broker-dealer and they should be designated Material Associated Persons. The next layer may consist of a corporate holding company which has a controlling interest in the broker-dealer holding company and often one or more other intermediate holding companies that engage in businesses independent of the broker-dealer. The reach of the proposed rules will, in some instances, extend farther than the broker-dealer's immediate parent and its affiliates. For example, other immediate holding

companies and the ultimate parent corporation may meet the material impact test. A potential bankruptcy filing by the ultimate parent company could directly threaten the broker-dealer's ability to obtain credit or might interfere with the broker-dealer's access to the clearance and settlement system. On the other hand, there may be situations where, after an evaluation of all the relevant circumstances, it appears that associated persons in the upper levels of the holding company hierarchy could have only a remote impact on the financial and operational condition of the broker-dealer and they should not therefore, be designated Material Associated Persons.

Another factor relevant to the materiality analysis is the overall funding needs of the broker-dealer and the degree, if any, to which the broker-dealer is financially dependent upon the associated person. Specifically, where a broker-dealer relies on the commercial paper or other unsecured credit of the holding company for financing, the broker-dealer would be materially affected by an acceleration or call by holders of such obligations because of events at the holding company level. These circumstances would be particularly troublesome if the broker-dealer, the holding company or other affiliates lacked sufficient liquid assets or alternative lines of credit to replace the unsecured financing. These conditions existed in the case of Drexel and its registered broker-dealer DBL.

The degree to which the broker-dealer or its customers rely on the associated person for operational services or support is also a factor. Merely offering products or services to the customers of a broker-dealer, such as the insurance products to brokerage customers will, by itself, not rise to the level of materiality called for by the proposed rules. However, if the broker-dealer relies on the associated person for significant operational facilities or services, the activities or financial troubles of the associated person may well have a material impact on the financial or operational condition of the broker-dealer. Within this category are those associated persons who provide financial services to customers of the broker-dealer, as in the case of an interest rate swap or a bridge loan arranged by an associated person in connection with underwriting or merger activities.

A fourth materiality factor is the level of risk present in the activities of the broker-dealer or its associated persons. For instance, some financial and securities activities, such as agency

¹⁵ Section 3(a)(18) of the Exchange Act, 15 U.S.C. 78c(a)(18), defines an "associated person of a broker or dealer" as "any partner, officer, director, or branch manager of such broker or dealer (or any person occupying a similar status or performing similar functions), any person directly or indirectly controlling, controlled by, or under common control with such broker or dealer, or any employee of such broker or dealer * * *"

¹⁶ See Section 17(h)(1) of the Act.

¹⁷ See H. Rep. 27.

securities transactions not involving margin lending or mutual fund distributions, involve lower degrees of risk than do merchant banking activities, commercial lending, insurance underwriting, proprietary trading, and venture capital activities. Consequently, associated persons that engage in activities associated with high degrees of risk are more likely to encounter financial difficulties, and are therefore more likely to have a material impact on the registered firm. Additionally, a relevant consideration in this category is the degree of leverage in the associated entity. Activities which by themselves do not entail a high level of risk become riskier when conducted with an inordinate degree of leverage.

Finally, the extent to which the associated person has the ability or the authority to cause a withdrawal of capital from the broker-dealer is a central consideration under the proposed rules. Where the holding company or an affiliate of a broker-dealer has the ability to remove capital from the firm, either in the form of dividends, other than routine dividends paid out of a portion of current operating profits, or repayment of debt or loans, that person's activities generally are material to the broker-dealer. The recordkeeping and reporting requirements of proposed Rules 17h-1T and 17h-2T would, in many cases, be triggered with respect to any associated person with such authority.

The Commission believes that broker-dealers should make the initial determination, based on overall facts and circumstances, of which associated persons are Material Associated Persons. Once the risk assessment program has commenced, the Commission will be able to oversee and evaluate the decisions made by each broker-dealer. The Commission believes that this approach is the most workable manner to provide guidance to the industry on this issue. Moreover, the Commission expects that the early stages of the risk assessment program will be characterized by a continuing dialogue between the broker-dealer community and the staff. Through this dialogue, the staff will be able to identify which entities should be included in the broker-dealer's risk assessment reports.

3. Filing Requirements

Proposed Rule 17h-1T specifies that a Form 17-H must be filed within forty-five days after the end of each of the broker-dealer's fiscal quarters. Broker-dealers may file the cumulative year-end financial statements within 90 days of the end of the fiscal year. In such a case,

the information regarding aggregate securities and commodities positions, real estate, and the other items included in Part II of Form 17-H would still have to be filed within 45 days of the fiscal year end. Proposed Rule 17h-2T also specifies that the material complied by broker-dealers must be preserved in accordance with the provisions of Rule 17a-4. For example, Rule 17a-4 requires that records must be maintained in a readily accessible place. Proposed Rule 17h-2T also requires broker-dealers to keep the information for a period of not less than three years. All information filed to the Commission pursuant to proposed Rule 17h-2T will be deemed confidential.

The Commission notes that the proposed rules contain a procedure available to holding companies that contain more than one registered broker-dealer. In these instances, the largest broker-dealer in the organization may apply to the Commission to be designated a "Reporting Broker or Dealer" for the purposes of the risk assessment rules. Once the Commission has designated a particular broker-dealer the Reporting Broker or Dealer for the organization, only the Reporting Broker or Dealer would be required to file risk assessment information with the Commission, and the other registered broker-dealers in the enterprise would be relieved of the filing burden.

4. Exemptions

The risk assessment provisions of the Reform Act were designed to give the Commission greater advance warning of situations, such as the Drexel failure, which could have a significant impact on the functioning of the markets and investors in general. The proposed risk assessment rules are intended to give the Commission access to the types of information that will alert the staff to potentially significant problems within a broker-dealer holding company. The Commission preliminarily believes that the majority of registered broker-dealers that conduct a business with the public do not pose the types of risks the Reform Act was designed to address.¹⁸ The Commission initially believes that the risk assessment program should include the segment of the industry that includes the broker-dealers that pose the greatest risks to customers and to the markets.¹⁹

¹⁸ According to the Senate Report, "It is anticipated that the SEC would seek to exempt from the recordkeeping and reporting requirements broker-dealers whose activities are *de minimis* in nature." S. Rept. at 58.

¹⁹ In actual practice, the Commission expects the staff to focus their efforts on the largest 50 broker-dealers.

Included in the group of brokers or dealers whose activities are not likely to pose a material threat to the investing public or the marketplace are the many limited purpose mutual fund brokers who are already exempt from the provisions of the customer protection rule. This category would include the firms associated with insurance companies that are registered with the Commission as broker-dealers in order to offer variable annuity and other insurance related products. The Commission believes these limited purpose firms are beyond the intended scope of the risk assessment program and therefore, proposes to exempt them from the rules.

Additionally, to limit the application of the rules to all but the most significant broker-dealers, the Commission is proposing an exemption for all broker-dealers that maintain capital including subordinated debt of less than \$5 million and who do not carry customer accounts.

Finally, any broker or dealer may, by application, request an individual exemption from the rules. Section 17(h) directs the Commission to consider a number of factors which have been incorporated into the draft rules. These include: The availability of information from another regulatory agency; the primary business of an associated person; the nature and extent of domestic or foreign regulation; the nature and extent of the broker-dealer's securities activities; and the amount of assets and revenues derived from and involved in United States securities activities. For example, it may be appropriate to relieve a particular broker-dealer or class of broker-dealers from the specific provisions of proposed Rule 17h-1T where comparable information is already maintained and copies thereof are filed pursuant to proposed Rule 17h2T.

Comment is requested on the proposed exemptive provisions, and specifically whether they should be expanded to include other groups of broker-dealers.

5. Special Provisions for Banks and Insurance Companies

The Commission recognizes that certain associated persons of broker-dealers are subject to the supervision of either a federal banking agency or a state insurance commissioner or similar official. To eliminate the need for banks and insurance companies to maintain two sets of records, the Commission is proposing special provisions for these entities.

With respect to a Material Associated Person that is subject to the supervision of a Federal banking agency, the proposed rules provide that broker-dealers may provide to the Commission copies of the reports filed with the appropriate banking regulator. The Commission notes that it has the authority to obtain more detailed call reports from the bank provided it first consults the federal banking agency to determine whether the information needed is available from such agency for other purposes, unless the Commission determines that any delay resulting from such consultation would be detrimental to the financial well-being of the broker-dealer.

The Commission is proposing similar provisions for Material Associated Persons subject to the supervision of a state insurance commissioner or similar official. Under the proposed rules, a Material Associated Person organized as a mutual insurance company would satisfy the risk assessment rules if the broker-dealer provides to the Commission copies of annual and quarterly reports filed by the parent insurance company with the state insurance regulator of the parent's domiciliary state. Additionally, mutual insurance companies would be required to maintain at the broker-dealer copies of the exhibits and the schedules to the annual and quarterly reports, together with copies of the annual and quarterly reports prepared by other affiliated insurance companies in the holding company structure. In the case of an insurance company organized as a stock company, the broker-dealer would be required to provide copies of the filings made by each Material Associated Person with the Commission under sections 13 or 15 of the Act, together with filings made under the Investment Company Act of 1940. The broker-dealer would be required to maintain, but not provide, copies of the annual and quarterly reports filed by such stock insurance companies with state insurance regulators. Additionally, where applicable, a brief reconciliation of the differences between the statutory accounting method used in the Annual and Quarterly Reports and GAAP is required.

III. Request for Comment

The Commission requests comment on the proposed rules and form. Commentators are invited to address the scope of the proposed risk assessment rules and the potential burdens imposed by them. The Commission solicits comments from broker-dealers regarding what types of risk assessment information they currently maintain.

In addition, the Commission requests comment on the approach and impact of the risk assessment rules on the broker-dealers that are owned by foreign entities and those broker-dealers owned by U.S. entities whose associated persons are regulated by U.S. regulatory entities. These firms should address the recordkeeping and reporting requirements imposed on their Material Associated Persons to enable the Commission to evaluate whether the information reported to foreign or domestic regulators would be sufficient for Commission risk assessment purposes. Specifically, the Commission requests comment on the form and content of the reports filed by associated persons of broker-dealers with other domestic or foreign regulators (such as Japan's Ministry of Finance).

The Commission also invites comment on the exemptive provisions of the proposed Rules. The Commission particularly requests comment whether a category of broker-dealers other than those proposed to be exempted in the rules should also be included.

Finally, the Commission requests comment on whether any additional requirement, rules or amendments to existing rules are appropriate to address the concerns raised by the development of complex holding company structures to which many brokers and dealers belong.

IV. Summary of Initial Regulatory Flexibility Analysis

The Commission has prepared an Initial Regulatory Flexibility Analysis ("IRFA") in accordance with 5 U.S.C. 630 concerning the proposed rules. The analysis notes that the objective of the proposed rules is to enable the Commission to obtain information concerning the risks to registered broker-dealers created by the business activities of the broker-dealer's holding company, affiliates, or subsidiaries. Smaller broker-dealers will generally not be affected by the proposed rules because the rules exempt from their requirements certain smaller entities. A copy of the IRFA may be obtained by contacting Roger G. Coffin, Division of Market Regulation, Securities and Exchange Commission, 450 Fifth Street, NW., Washington DC, 20549, (202) 272-2396.

V. Statutory Analysis

Pursuant to the Securities Exchange Act of 1934 and particularly sections 17 and 23 thereof, 15 U.S.C. 78q and 78w, the Commission proposes to add a new 240.17h-1T and 240.17h-2T, to title 17 of the Code of Federal Regulations in the manner set forth below.

List of Subjects in 17 CFR Parts 240 and 249

Reporting and recordkeeping requirements; Securities.

VI. Text of the Proposed Rules

In accordance with the foregoing, title 17, chapter II of the Code of Federal Regulations is proposed to be amended as follows:

PART 240—GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE ACT OF 1934

1. The authority citation for part 240 is amended by adding the following citation:

Authority: 15 U.S.C. 77c, 77d, 77a, 77(t), 78c, 78d, 78i, 78j, 78l, 78m, 78n, 78o, 78p, 78a, 78w, 78x, 79q, 79t, 80a-29, 80a-37, unless otherwise noted.

* * * * *

240.17h-1T also issued under 15 U.S.C. 78q.

2. By adding § 240.17h-1T to read as follows:

§ 240.17h-1T Risk Assessment Recordkeeping Requirements for Associated Persons of Brokers and Dealers.

(a) *Requirement to maintain and preserve information.* (1) Every broker or dealer registered with the Commission pursuant to section 15 of the Act, and every municipal securities dealer registered pursuant to section 15B of the Act for which the Commission is the appropriate regulatory agency, unless exempt from the provisions of this section pursuant to paragraph (c) of this section, shall maintain and preserve the following information:

(i) An organizational chart which includes the broker or dealer and all its associated persons, together with a flow chart of the organization's consolidation process. The organizational chart shall reflect all material business lines conducted by the broker or dealer and the associated persons of the broker or dealer. Included in the organizational chart shall be a designation of which associated persons are Material Associated Persons;

(ii) Written policies, procedures, or standards concerning the credit controls and the extension of credit, including collateral procedures of each Material Associated Person;

(iii) Written policies, procedures, or standards concerning the financing of each Material Associated Person, including information regarding bank loans, repurchase agreements, stock loans, commercial paper, medium-term and long-term notes, subordinated debt

and the issuance of equity or preferred stock;

(iv) Written policies, procedures, or standards concerning the financing trading risks assumed by each Material Associated Person, including records regarding reporting responsibilities for trading activities, policies relating to restrictions or limitations on trading securities and financial instruments or products, and a description of the types of reviews conducted to monitor existing positions, and limitations or restrictions on trading activities;

(v) A description of all material pending legal or arbitration proceedings that are required to be disclosed under generally accepted accounting principles to which any Material Associated Person is a party, or of which any of its property is the subject; and

(vi) Information regarding the capital adequacy of each Material Associated Person, including a brief narrative discussion by management of the liquidity of the material assets, the structure of debt capital, and sources of alternative funding.

(2) Every broker or dealer registered with the Commission pursuant to section 15 of the Act, and every municipal securities dealer registered pursuant to section 15B of the Act for which the Commission is the appropriate regulatory agency, unless exempt from the provisions of paragraph (a) pursuant to paragraph (c) of this section, shall maintain and preserve the following records:

(i) Consolidated and consolidating balance sheets, prepared in accordance with generally accepted accounting principles, as of the end of the quarter for the broker or dealer and each Material Associated Person. For the purposes of paragraphs (a)(2) (i) and (ii) of this section, broker or dealer shall include its ultimate holding company or parent;

(ii) Quarterly consolidated and consolidating income statements and consolidated cash flow statements, prepared in accordance with generally accepted accounting principles, for the broker or dealer and each Material Associated Person;

(iii) The amount at the end of the quarter, and the highest and lowest amounts during the quarter, of the aggregate securities and commodities positions, together with limited partnership interests held by each Material Associated Person, including a separate listing of each single unhedged securities or commodities position, other than U.S. government and agency securities, that exceeds the Materiality Threshold at any time during the quarter;

(iv) The amount at the end of the quarter, and the highest and lowest amounts during the quarter, of the aggregate notional or contractual amounts of, and the gross payments owed under, any interest rate, currency, commodity or stock index swaps, or other similar financial instruments with off-balance sheet risk (as defined in Statement of Financial Accounting Standards No. 105), where the Material Associated Person incurs principal risk or otherwise operates a trading book, not including commitments made in connection with non-securities or non-financial activities, with a separate entry of each commitment where the notional or contractual amount exceeds the Materiality Threshold at any time during the quarter;

(v) The amount at the end of the quarter, and the highest and lowest amounts during the quarter, of the aggregate amount of the bridge loans and material unsecured extensions of credit with an initial or remaining maturity of less than one year by each Material Associated Person, together with the allowance for losses for such transactions, including a specific description of any extensions of credit to a single borrower exceeding the Materiality Threshold at any time during the quarter;

(vi) The amount at the end of the quarter, and the highest and lowest amounts during the quarter, of the aggregate amount of material extensions of credit, loans or advances, whether secured or unsecured, between by each Material Associated Persons to other associated persons of the broker or dealer, whether or not designated Material Associated Persons, including a specific description of any transaction that exceeds the Materiality Threshold at any time during the quarter;

(vii) The amount at the end of the quarter, and the highest and lowest amounts during the quarter, of the aggregate amount of the commercial paper, material unsecured borrowing, other material short-term financings scheduled to mature within one year, and the principal installments of long-term or medium-term debt scheduled to mature within one year;

(viii) The amount at the end of the quarter, and the highest and lowest amounts during the quarter, of the aggregate amount of material investments in equity, debt or any other commitments to invest in any affiliated companies by each Material Associated Person;

(ix) Aggregate data relating to real estate activities, including mortgage loans and investments in real estate

conducted by each Material Associated Person, including:

(A) The Material Associated Person's lending and risk management policies and procedures, including minimum loan-to-appraised value ratios;

(B) The types of properties securing loans and investments and the amounts of loans and investments secured by each type;

(C) The geographic distribution, as of the end of the quarter, by amount of such loans or investments and the year such loans were made (with all loans made in the previous five years being a single category);

(D) The Material Associated Person's policy for placing loans on non-accrual status;

(E) The aggregate carrying value of mortgage loans which are not current as to interest or principal, which are in the process of foreclosure, have been restructured, or where a required payment has not been made within 60 days of the date such payment was due;

(F) The allowance for losses on mortgage loans and on investment real estate by category; and the activity in the allowance for losses account; and

(G) Information about risk concentration in the investment real estate and the mortgage loan portfolio, including, without limitation, information about risk concentration to a single borrower, location or property; and

(x) The amount at the end of the quarter and the highest and lowest amounts during the quarter of all material leases financing activities of each Material Associated Person, including a description of and a breakdown of the types of leases outstanding, together with the aggregate amounts of leases where a required payment has not been made within 60 days of the date such payment was due.

(3) The determination of whether an associated person of a broker or dealer is a Material Associated Person shall involve consideration of all aspects of the activities of, and the relationship between, both entities, including without limitation, the following factors:

(i) The legal relationship between the broker or dealer and the associated person;

(ii) The overall financing requirements of the broker or dealer and the associated person, and the degree, if any, to which the broker or dealer and the associated person are financially dependent on each other;

(iii) The degree, if any, to which the broker or dealer or its customers rely on the associated person for operational

support or services in connection with the broker's or dealer's business;

(iv) The level of risk present in the activities of the broker or dealer or of any of the broker's or dealer's associated persons; and

(v) The extent to which the associated person has the authority or the ability to cause a withdrawal of capital from the broker or dealer.

(4) For the purposes of this rule, the term financial and securities activities shall include, without limitation, principal and agency transactions involving equity or debt securities, futures, forward transactions, forward and spot market commodity transactions, commercial paper brokering, purchases of financial assets for securitization and subsequent sale as securities, merchant banking activities, bridge loan transactions, insurance transactions (other than activities that are actuarial determinations of mortality or other risks or loss reserves, or insurance underwriting activities ensuring a distribution of policy holder risk), lending, activities, real estate development, and taking principal risk or otherwise operating a trading book in connection with the exchange of interest rate or foreign currency obligations. The term financial and securities activities shall not include manufacturing, construction (other than equity investments or financing, merchandising, travel services, real estate brokerage, consumer lending, publishing, or non-securities related information processing.

(5) The information, reports and records required by the provisions of this section shall be maintained and preserved in accordance with the provisions of Rule 17a-4 (17 CFR 240.17a-4) and shall be kept for a period of not less than three years in an easily accessible place.

(6) For the purpose of this section and § 240.17h-2T, the term *Materiality Threshold* shall mean the greater of:

(i) \$100 million; or

(ii) 10 percent of the broker or dealer's tentative net capital based on the most recently filed Form X-17A-5 or 10 percent of the Material Associated Person's tangible net worth, whichever is greater.

(b) *Special provisions with respect to material associated persons subject to the supervision of a Federal banking agency or an insurance commissioner or other similar official or agency of a State.* A broker or dealer shall be deemed to be in compliance with the recordkeeping requirements of paragraph (a) of this section with respect to a Material Associated Person if:

(1)(i) Such Material Associated Person is subject to examination by, and the reporting requirements of, a Federal banking agency; and

(ii) The broker or dealer maintains in accordance with the provisions of § 240.17h-2T copies of reports submitted by such Material Associated Person with the Federal banking agency pursuant to section 5211 of the Revised Statutes, section 9 of the Federal Reserve Act, section 7(a) of the Federal Deposit Insurance Act, section 10(b) of the Home Owners' Loan Act, or section 8 of the Bank Holding Company Act of 1956; or

(2)(i) If such Material Associated Person is subject to the supervision of an insurance commissioner or other similar official or agency of a state; and

(ii) In the case of a Material Associated Person organized as a stock company, the broker or dealer:

(A) Maintains in accordance with the provisions of § 240.17h-2T copies of the Annual and Quarterly Statements with Schedules and Exhibits prepared by the insurance company on forms prescribed by the insurance company's domiciliary state; and

(B) Furnishes in accordance with the provisions of § 240.17h-2T copies of the filings made by the insurance company pursuant to section 13 or 15 of the Act and the Investment Company Act of 1940; or

(iii) In the case of a Material Associated Person organized as a mutual insurance company, the broker or dealer:

(A) Maintains in accordance with the provisions of § 240.17h-2T copies of the Annual and Quarterly Statements with Schedules and Exhibits prepared by insurance companies other than the parent insurance company on forms prescribed by such insurance companies' domiciliary state; and

(B) Furnishes in accordance with the provisions of § 240.17h-2T copies of the Annual and Quarterly Statements prepared by the parent insurance company on forms prescribed by the parent insurance company's domiciliary state. The Annual Statement shall include: the classification (distribution by state) section from the schedule of real estate; distribution by state, the interest overdue (more than 90 days), in process of foreclosure, and foreclosed properties transferred to real estate during the year sections from the schedule of mortgage; and the quality and maturity distribution of all bonds at statement values and by major types of issues section from the schedule of bonds and stocks. All other Schedules and Exhibits to such Annual and Quarterly Statements shall be

maintained at the broker-dealer but not filed with the Commission; and

(C) Furnishes a reconciliation of the statutory financial statements contained in the Annual and Quarterly Statements to the consolidated financial statements required by Generally Accepted Accounting Principles if such reconciliation is provided to an insurance commissioner or other similar official or agency of a state.

(iv) If the event an insurance company organized as a stock or mutual company is not required to prepare Quarterly Statements, the broker or dealer must maintain and preserve the records required by paragraph (a) of this section on a quarterly basis.

(c) *Exemptions.* (1) The Commission may, upon written application, exempt from the provisions of this section, either unconditionally or on specified terms and conditions, any broker or dealer which satisfies the Commission that it is not necessary in the public interest or for the protection of investors to subject the broker or dealer to the provisions of this section. In granting exemptions under paragraph (c)(1) of this section, the Commission shall consider, among other factors:

(i) Whether information of the type required to be maintained and preserved by this section is currently available from a supervisory agency, a state insurance commission or similar state agency, the Commodity Futures Trading Commission or a foreign regulatory agency or body;

(ii) The primary business engaged in by the associated person or persons of the broker or dealer;

(iii) The nature and extent of domestic or foreign regulation of the associated person or persons of the broker or dealer;

(iv) The nature and extent of the broker or dealer's securities activities; and

(v) The amount and proportion, on a consolidated basis, of assets of the broker or dealer and its associated persons, devoted to, and revenues derived from, activities in the United States securities markets.

(2) The provisions of this section shall not apply to any broker or dealer which is exempt from the provisions of Rule 15c3-3 of the Act pursuant to paragraph (k)(1) thereof and limits its activities to the purchase, sale and redemption of redeemable securities of registered investment companies or of interests or participations in an insurance company separate account, whether or not registered as an investment company; the solicitation of share accounts for savings and loan institutions insured by

an instrumentality of the United States; and the sale of securities for the account of a customer to obtain funds for immediate reinvestment in redeemable securities of registered investment companies.

(3) The provisions of this section shall not apply to any broker or dealer which:

(i) Maintains capital including debt subordinated in accordance with appendix D of Rule 15c3-1 of the Act of less than \$5,000,000; and

(ii) Does not hold funds or securities for, or owe money or securities to, customers and does not carry the accounts of or for customers.

(iii) In calculating capital for the purposes of this paragraph, a broker or dealer shall include the equity capital and subordinated debt of any other registered brokers or dealers that are associated with the broker or dealer and are not otherwise exempt from the provisions of this section.

(4) The Commission may, upon written application by a Reporting Broker or Dealer, exempt from the provisions of this section, either unconditionally or on specified terms and conditions, any brokers or dealers associated with such Reporting Broker or Dealer. The term "Reporting Broker or Dealer" shall mean, in the case of a broker or dealer that is associated with other registered brokers or dealers, the broker or dealer which maintains the greatest amount of net capital as reported on its most recently filed Form X-17A-5. In granting exemptions under paragraph (c)(4) of this section, the Commission shall consider, among other factors, whether the records and other information required to be maintained pursuant to this section concerning the Material Associated Persons of the broker or dealer associated with the Reporting Broker or Dealer will be available to the Commission pursuant to § 240.17h-2T

(d) Confidentiality. All information obtained by the Commission pursuant to the provisions of this section from a broker or dealer concerning a Material Associated Person shall be deemed confidential information for the purposes of section 24(b) of the Act.

3. By adding § 240.17h-2T to read as follows:

§ 240.17h-2T Risk Assessment Reporting Requirements for Brokers and Dealers.

(a) *Reporting requirements of risk assessment information required to be maintained by § 240.17h-1T.* (1) Every broker or dealer registered with the Commission pursuant to section 15 of the Act, and every municipal securities dealer registered pursuant to section 15B of the Act for which the Commission is

the appropriate regulatory agency, unless exempt from this section pursuant to paragraph (b) of this section, shall file a Form 17-H within 45 calendar days after the end of each fiscal quarter. The Form 17-H for the fourth fiscal quarter shall be filed within 45 calendar days of the end of the fiscal year; however, the cumulative year-end financial statements required by § 240.17h-1T may be filed separately within 90 calendar days of the end of the fiscal year.

(2) The reports required to be filed by paragraph (a)(1) of this section shall be considered filed when received at the Commission's principal office in Washington, DC.

(3) For the purposes of this section, the term Material Associated Person shall have the meaning used in § 240.17h-1T.

(b) *Exemptions.* (1) The Commission may, upon written application, exempt from the provisions of this section, either unconditionally or on specified terms and conditions, any broker or dealer that satisfies the Commission that it is not necessary in the public interest or for the protection of investors to subject the broker or dealer to the provisions of this section. In granting exemptions under this paragraph, the Commission shall consider, among other factors:

(i) Whether information of the type required to be maintained and preserved pursuant to the provisions of § 240.17h-1T is currently available from a supervisory agency, a state insurance commission or similar state agency, the Commodity Futures Trading Commission or a foreign regulatory agency or body;

(ii) The primary business engaged in by the associated person or persons of the broker or dealer;

(iii) The nature and extent of domestic or foreign regulation of the associated person or persons of the broker or dealer;

(iv) The nature and extent of the broker or dealer's securities activities; and

(v) The amount and proportion, on a consolidated basis, of assets of the broker or dealer and its associated persons devoted to, and revenues derived from, activities in the United States securities markets.

(2) The provisions of this section shall not apply to any broker or dealer which is exempt from the provisions of § 240.15c3-3 of the Act pursuant to paragraph (k)(1) thereof and limits its activities to the purchase, sale and redemption of redeemable securities of registered investment companies or of interests or participations in an

insurance company separate account, whether or not registered as an investment company; the solicitation of share accounts for savings and loan institutions insured by an instrumentality of the United States; and the sale of securities for the account of a customer to obtain funds for immediate reinvestment in redeemable securities and registered investment companies.

(3) The provisions of this section shall not apply to any broker or dealer which:

(i) Maintains capital including debt subordinated in accordance with appendix D of Rule 15c3-1 of the Act of less than \$5,000,000; and

(ii) Does not hold funds or securities for, or owe money or securities to, customers and does not carry the accounts of or for customers.

(iii) In calculating capital and subordinated debt for the purposes of paragraph (b) of this section, a broker or dealer shall include the equity capital and subordinated debt of any other registered brokers or dealers that are associated with the broker or dealer and are not otherwise exempt from the provisions of this section.

(4) The Commission may, upon written application by a Reporting Broker or Dealer, exempt from the provisions of this section, either unconditionally or on specified terms and conditions, any brokers or dealers associated with the Reporting Broker or Dealer. The term "Reporting Broker or Dealer" shall mean, in the case of a broker or dealer that is associated with other registered brokers or dealers, the broker or dealer which maintains the greatest amount of net capital as reported on its most recently filed Form X-17A-5. In granting exemptions under paragraph (b)(4) of this section, the Commission shall consider, among other factors, whether the records and other information required to be maintained pursuant to § 240.17h-1T concerning the Material Associated Persons of the broker or dealer associated with the Reporting Broker or Dealer will be available to the Commission pursuant to the provisions of this section.

(c) *Special provisions with respect to material associated persons subject to the supervision of a Federal banking agency or an insurance commissioner or other similar official or agency of a State.* A broker or dealer shall be deemed to be in compliance with the reporting requirements of paragraph (a) of this section with respect to a Material Associated Person if:

(1)(i) Such Material Associated Person is subject to examination by and the reporting requirements of a Federal banking agency; and

(ii) The broker or dealer furnishes in accordance with paragraph (b) of this section copies of reports filed by the Material Associated Person with the Federal banking agency pursuant to section 5211 of the Revised Statutes, section 9 of the Federal Reserve Act, section 7(a) of the Federal Deposit Insurance Act, section 10(b) of the Home Owners' Loan Act, or section 8 of the Bank Holding Company Act of 1956; or

(2)(i) If the Material Associated Person is subject to the supervision of an insurance commissioner or other similar official agency of a state; and

(ii) In the case of a Material Associated Person organized as a stock company, the broker or dealer:

(A) Maintains in accordance with the provisions of this section copies of the Annual and Quarterly Statements with Schedules and Exhibits prepared by the insurance company on forms prescribed by the insurance company's domiciliary state; and

(B) Furnishes in accordance with the provisions of this section copies of the filings made by the insurance company pursuant to sections 13 or 15 of the Act and the Investment Company Act of 1940; or

(iii) In the case of a Material Associated Person organized as a mutual insurance company, the broker or dealer:

(A) Maintains in accordance with the provisions of this section copies of the Annual and Quarterly Statements with Schedules and Exhibits prepared by insurance companies other than the parent insurance company on forms prescribed by such insurance companies' domiciliary state; and

(B) Furnishes in accordance with the provisions of this section copies of the Annual and Quarterly Statements prepared by the parent insurance company on forms prescribed by the parent insurance company's domiciliary state. The Annual Statement shall include: The classification (distribution by state) section from the schedule of real estate; distribution by state, the interest overdue (more than three months), in process of foreclosure, and foreclosed properties transferred to real estate during the year sections from the schedule of mortgages; and the quality and maturity distribution of all bonds at statement values and by major types of issues section from the schedule of bonds and stocks. All other Schedules and Exhibits to such Annual and Quarterly Statements shall be maintained at the broker-dealer but not furnished to the Commission; and

(C) Furnishes in accordance with the provisions of this section a reconciliation of the statutory financial

statements contained in the Annual and Quarterly Statements to the consolidated financial statements required by GAAP if such reconciliation is provided to an insurance commissioner or other similar official or agency of a state.

(iv) In the event an insurance company organized as a stock or mutual company is not required to prepare Quarterly Statements, the broker or dealer must file with the Commission a Form 17-H in accordance with the provisions of this section on a quarterly basis.

(3) No broker or dealer shall be required to furnish to the Commission any examination report of any Federal banking agency or any supervisory recommendations or analyses contained therein with respect to a Material Associated Person that is subject to the regulation of a Federal banking agency.

(4) The furnishing of any information or documents by a broker or dealer pursuant to this section shall not constitute an admission for any purpose that a Material Associated Person is otherwise subject to the Act. Any documents or information furnished to the Commission by a broker or dealer pursuant to this rule shall not be deemed to be "filed" for the purposes of the liabilities set forth in section 18 of the Act.

(d) Confidentiality. All information obtained by the Commission pursuant to the provisions of this section from a broker or dealer concerning a Material Associated Person shall be deemed confidential information for the purposes of section 24(b) of the Act.

PART 249—FORMS, SECURITIES EXCHANGE ACT OF 1934

4. The authority citation for part 249 continues to read as follows:

Authority: 15 U.S.C. 78a, et seq., unless otherwise noted.

5. By adding § 249.328T to read as follows:

§ 249.328T Form 17-H, Risk Assessment Report for Brokers and Dealers pursuant to section 17(h) of the Securities Exchange Act of 1934 and rules thereunder.

This form shall be used by brokers and dealers in reporting information to the Commission concerning certain of their associated persons pursuant to section 17(h) of the Securities Exchange Act of 1934 (15 U.S.C. § 78q(h)) and Rules 17h-1T and 17h-2T thereunder (§§ 240.17h-1T and 240.17h-2T of this chapter).

Note: Appendix A will not appear in the Code of Federal Regulations.

Appendix A

*Securities and Exchange Commission,
Washington, DC 20549*

Form 17-H Risk Assessment Report for Brokers and Dealers

Part I

Risk Assessment Reporting Requirements for Brokers and Dealers

Report at the close of business as of the last day of the fiscal quarter.

This report is to be filed within 45 calendar days of the end of each fiscal quarter by brokers and dealers concerning each Material Associated Person (as defined in Temporary Rules 17h-1T and 17h-2T). The report for the fourth fiscal quarter shall be filed within 45 calendar days of the end of the fiscal year but the cumulative year end financial statements may be filed separately within 90 days of the end of the fiscal year.

In the event a broker or dealer is associated with one or more other registered broker or dealers, each broker or dealer is required to file a separate Form 17-H. The Commission, however, may exempt from the filing requirements all brokers or dealers associated with a broker or dealer that has been designated a "Reporting Broker or Dealer." The term "Reporting Broker or Dealer" shall have the meaning set forth in Rules 17h-1T and 17h-2T. A broker or dealer seeking designation as a Reporting Broker or Dealer must apply to the Commission for an exemption pursuant to paragraph (b)(5) of Rule 17h-2T. Pending such designation, each broker or dealer associated with the broker or dealer requesting such designation is required to file a separate Form 17-H.

Name of Reporting Broker-Dealer

SEC File No.

Name of Associated Broker-Dealer not Filing (If applicable)

Address of Principal Place of Business

Firm I.D. No.

For Period Beginning (MM/DD/YY)

And Ending (MM/DD/YY)

Name and Telephone Number of Person to Contact in Regard to This Report

Name(s) of Material Associated Persons Contained in This Report:

Attention

Intentional misstatements or omissions of facts constitute Federal Criminal Violations. See 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).

Intentional misstatements or omissions of facts may also result in civil fines and other sanctions pursuant to section 20 of the Securities Exchange Act of 1934.

The person signing this report represents hereby that all information contained in this Form is true, correct and complete. It is understood that all information in this Form is considered an integral part of this Form and that the submission of any amendment represents that all unamended information remains true, correct and complete as previously filed.

Pursuant to the Securities Exchange Act of 1934, the undersigned has caused this report to be signed on its behalf in the City of _____ and State of _____ on the ____ day of _____, 19____.

(Name of Broker-Dealer)

(Signature and Title of Person Duly Authorized to Submit This Report)

General Information and Instructions

Note: In completing this Form, the broker-dealer should reflect its operations in the consolidated and consolidating financial statements. The broker-dealer should not include information concerning its activities in the information required by Part II of this Form if such information is filed with the Commission as part of the broker-dealer's Form X-17A-5 or Form G-405. The information required by Part II of this Form should be completed separately for each such Material Associated Person, even if the financial information contained in a broker-dealer's Form X-17A-5 includes information concerning non-broker-dealer associated persons which are designated Material Associated Persons.

Item 1. Organizational Chart Reflecting the Associated Persons and the Broker-Dealer

1. Provide an organizational chart which includes the broker-dealer and its associated persons.

2. Provide a statement of:

a. Which associated persons are Material Associated Persons, together with a brief narrative discussion about the criteria used in making the assessment as to which entities are Material Associated Persons;

b. Business line(s) conducted by each Material Associated Person; and

c. The names of the President and the Chief Financial Officer of each Material Associated Person.

3. The information provided pursuant to this Item should be included in the first Form 17-H filed by the broker-dealer and in the year end filing. Quarterly updates should be provided only where a material change in the information provided to the Commission has occurred.

Item 2. Risk Management and Other Policies

1. Provide copies of the risk management and other policies maintained by the broker-dealer pursuant to paragraphs (a)(1) (ii) through (iv) of § 240.17h-1T.

2. The information provided pursuant to this Item should be included in the first Form 17-H filed by the broker-dealer. Quarterly updates should be provided only where a material change in the information provided to the Commission has occurred.

Item 3. Legal Proceedings

1. Provide a brief description of any material pending legal or arbitration proceedings that are required to be disclosed under generally accepted accounting principles to which any Material Associated Person is a party, or of which any of its property is the subject.

2. The information provided pursuant to this Item should be included in the first Form 17-H filed with the Commission. Quarterly updates should be provided only where a material change in the information provided to the Commission has occurred.

Item 4. Capital Adequacy Information

1. Provide the information required by paragraph (a)(1)(vi) of § 240.17h-1T, including a narrative statement describing the current aggregate amounts and sources of funding for the broker or dealer and each Material Associated Person.

2. The information provided pursuant to this Item should also include a separate statement of the potential alternative borrowing sources that would be available to the broker or dealer and each Material Associated Person in the event of a major market disturbance. For the purposes of this Item, the term "major market disturbance" shall refer to events characterized by sudden and extreme fluctuations of securities prices generally, or a substantial threat thereof, or other substantial disruption of the operation of the credit markets or the domestic and international banking system. This information should include

the nature and history of banking relationships; the quality, liquidity, and maturity of investment portfolios and amounts of cash on hand; normal and expected operating cash requirements; the degree of reliance on commercial paper and other short-term funding sources; the amount of unencumbered liquid securities that may be pledged to obtain secured loans; the availability of committed bank lines of credit; and whether these alternative borrowing sources are at a reasonable level in relation to short-term unsecured borrowing needs.

3. The information provided pursuant to this Item should be included in the first Form 17-H filed by the broker-dealer. Quarterly updates should be provided only where a material change in the information provided to the Commission has occurred.

Item 5. Financial Statements

Consolidated Financial Statements

1. For each quarterly and annual period required, provide consolidated and consolidating financial statements of the parent company and its subsidiaries. This information should depict the company on a total entity basis. The column headings of the consolidating financial statements should indicate the name of each Material Associated Person included in the financial statements and should include the registered broker-dealer.

2. The financial statements presented should be prepared in the form and content required by Regulation S-X, except as otherwise noted, and should include the following:

- a. Balance sheet;
- b. Statement of income;
- c. Statement of cash flows; and
- d. Notes to the financial statements.

3. Instructions to the financial statements.

a. The consolidated and consolidating financial statements should cover the company on a total entity basis to enable a reader to assess the overall financial condition of the broker-dealer and each Material Associated Person. The broker-dealer may combine associated persons that do not have significant operating activities in a separate column in the financial statements. All other associated persons should be presented separately in the consolidating financial statements. The financial statements should be prepared using the applicable guidelines governing balance sheets and income statements set forth in Regulation S-X except as otherwise noted herein.

b. The financial statements should be prepared in accordance with generally accepted accounting principles in the United States ("U.S. GAAP"). With respect to associated persons that use a comprehensive set of accounting principles other than U.S. GAAP, a reconciliation to the U.S. GAAP should be included in a note to the financial statements. The note shall indicate the comprehensive body of accounting principles noted to prepare the financial statements. The reconciliation to U.S. GAAP may, however, be limited to income from continuing operations before income taxes and the equity portion of the balance sheet. The reconciliation should provide a narrative description of the items that are treated differently by U.S. GAAP and should quantify such items if the Material Associated Person is required to prepare a quantitative comparison to U.S. GAAP under any applicable federal law.

c. The financial statements should be accompanied by the footnotes required by GAAP and any other information necessary for an understanding of the information being presented (e.g., summary of significant accounting policies). The additional footnotes required by Regulation S-X but not required by GAAP may be omitted.

d. The notes to the financial statements required by GAAP should be provided only for the consolidated financial information. Footnote disclosure which would substantially duplicate the disclosure contained in the most recent annual consolidated financial statements may be omitted from the quarterly financial statements.

e. The quarterly information should contain sufficient disclosures and footnotes to make the information presented therein not misleading and should encompass any significant changes in accounting policies or capital structure since the end of the most recent fiscal year. In this regard, the guidelines in § 210.10-01(a)(5) of Regulation S-X for interim financial statements should be followed.

f. The statement of cash flows should be provided only for the consolidated financial statements. A statement of cash flows should be provided for the quarterly consolidated financial statements, but may be abbreviated in the following manner. The category for cash provided by operations may be condensed into a single item of net cash provided by operations. The categories for investing activities and financing activities must, however, include the significant activities that have occurred during the quarter.

g. Pro forma financial information should be presented to give effect to material transactions that took place during the year or subsequent to the date of the financial information being presented, as if they took place at the beginning of the fiscal year, if such information is necessary to understand the financial statements.

h. Quarterly information may be presented on an unaudited basis. In the event that a Material Associated Person normally prepares a consolidated audited year-end financial statement, the audited consolidated financial statements should be provided and shall include a manually signed accountant's report as required by § 210.2-02(a)(2) of Regulation S-X. In all other cases, the annual consolidated and consolidating financial statements which cover the full fiscal year may be presented on an unaudited basis in the report.

i. The quarterly financial statements should include information for the current quarter and the year-to-date. Comparative financial statements for the prior fiscal year should also be provided for the consolidated financial information.

j. If financial statements that are substantially the same as those required by this Form are filed with other regulatory bodies (e.g., banking regulatory agencies, state insurance departments, foreign regulators, other divisions of the Securities and Exchange Commission, etc.) those financial statements will be considered in whole or in part, to meet the requirements of this Form. For example, copies of the annual report on Form 10-K and quarterly report on Form 10-Q could be provided as an exhibit to Form 17-H in order to meet the consolidated financial statement requirement. However, because the financial statements contained in Forms 10-Q and 10-K are consolidated, consolidating financial statements must still be provided separately.

Item 6. Aggregate Securities and Commodities Positions

1. Provide a separate statement of the long and short aggregate securities and commodities positions held, as of the end of the quarter, by each Material Associated Person, using a separate column for each Material Associated Person. Include a separate statement of each security or commodity position that exceeds the Materiality threshold at any time during the quarter.

2. For the purposes of this Form, the term "Materiality Threshold" shall have the meaning set forth in section 240.17h-1T.

3. If a Material Associated Person or the broker-dealer calculates its exposure or risks incurred with respect to securities or commodities positions using a delta or similar analysis, a summary of that analysis should be provided.

Item 7. Financial Instruments With Off-Balance Sheet Risk

1. Provide a statement for the financial instruments with off-balance sheet risk (as that term is used in Statement of Financial Accounting Standards No. 105) held by each Material Associated Person as of the end of the quarter. Include a separate statement of each financial instrument with off-balance sheet risk that exceeds the Materiality Threshold at any time during the quarter.

2. If a Material Associated Person or the broker-dealer calculates its exposure or risks incurred with respect to financial instruments with off-balance sheet risk using a delta or similar analysis, a summary of this analysis should be provided.

3. Provide a narrative statement of management's analysis of the potential risk to the broker-dealer caused by financial instruments with off-balance sheet risk.

Item 8. Real Estate

1. Provide a statement of the material real estate investments held by each Material Associated Person.

2. Provide management's analysis, and where applicable, the amount of: (1) The mortgage loans where a required payment has not been made within 60 days of the date such payment was due together with loans considered to be potential problems; (2) the geographic distribution and year each material loan or investment was made with all loans or investments made before 1965 aggregated as a single category; (3) individual risk concentration and credit risk; (4) the loan to value ratios for the previous five years; and (5) the allowance for losses account.

Item 9. Investments in Other Companies

1. Provide a statement of each Material Associated Person's material investments in other companies as of the end of the quarter. Include a separate statement of each individual investment that exceeds the Materiality Threshold at any time during the quarter.

2. Provide a statement of each Material Associated Person's policies with respect to investments in other companies. Include in this statement management's assessment of the

liquidity of the investments, the risks and any other relevant information bearing on the potential impact of these investments on the registered broker-dealer.

3. The policy statement provided pursuant to this Item should be included in the first Form 17-H filed by the broker-dealer. Quarterly updates should be made only where a material change in the information provided to the Commission has occurred.

Part II

Provide the following balances for each material associated person as of the end of the quarter. Balances exceeding the materiality threshold at any time during the quarter should be separately indicated under the appropriate heading.

General Instructions

1. Indicate the name of each Material Associated Person and its major business activity in the columns. Groups of related subsidiaries that are engaged in similar business activities may be combined.

2. If any of the information that is requested in this Part is provided in the financial statements provided in response to Item 5, the information need not be repeated. A note should indicate where the information can be found (for example, see footnote 4 to the consolidated financial statements).

Aggregate Securities and Commodities Positions

1. U.S. Treasury securities
2. U.S. Government agency
3. Securities issued by states and political subdivisions in the U.S.
4. Foreign securities:
 - (a) Debt securities
 - (b) Equity securities
5. Banker's acceptances
6. Certificates of deposit
7. Commercial paper
8. Corporate obligations
9. Stocks and warrants (other than arbitrage positions)
10. Arbitrage:
 - (a) Index arbitrage and program trading
 - (b) Risk arbitrage
 - (c) Other arbitrage
11. Options:
 - (a) Market value of put options:
 - (i) Short-term options (expiration date of less than 6 months):
 - (A) Listed
 - (B) Unlisted
 - (ii) Long-term options:
 - (A) Listed
 - (B) Unlisted
 - (b) Market value of call options:
 - (i) Short-term options:
 - (A) Listed
 - (B) Unlisted
 - (ii) Long-term options:
 - (A) Listed

- (B) Unlisted
12. Spot commodities
13. Investments with no ready market:
 - (a) Equity
 - (b) Debt
 - (c) Other (include limited partnership interests)
14. Other securities or commodities
15. Summary of delta or similar analysis (if available)

Financial Instruments With Off-Balance Sheet Risk

1. When-issued securities:
 - (a) Gross commitments to purchase
 - (b) Gross commitments to sell
2. Interest rate contracts:
 - (a) Futures and forward contracts (e.g., U.S. Treasury securities futures, forward rate agreements and forward agreements on U.S. government securities)
 - (b) Option contracts (e.g., options on U.S. Treasury securities)
3. Written stock option contracts:
 - (a) Market value of short-term contracts:
 - (i) Listed
 - (ii) Unlisted
 - (b) Market value of long-term contracts:
 - (i) Listed
 - (ii) Unlisted
4. Purchased stock option contracts:
 - (a) Market value of short-term contracts:
 - (i) Listed
 - (ii) Unlisted
 - (b) Market value of long-term contracts:
 - (i) Listed
 - (ii) Unlisted
5. Interest rate swaps:
 - (a) Total notional or contractual value of interest rate swaps
 - (b) Total gross payments owed under interest rate swaps
 - (c) Per counterparty breakdown where the total notional amounts of the agreements with a single counterparty exceeds the Materiality Threshold
6. Foreign exchange rate swaps (e.g., cross currency swaps)
 - (a) Total notional or contractual value of foreign exchange rate swaps
 - (b) Total gross payments owed under exchange rate swaps
 - (c) Per counterparty breakdown where the total notional amounts of the agreements with a single counterparty exceeds the Materiality Threshold
7. All other swap agreements (e.g., oil swaps):
 - (a) Total notional or contractual value of all other swap agreements
 - (b) Total gross payments under all other swap agreements
 - (c) Per counterparty breakdown where the total notional amounts of the agreements with a single counterparty exceeds the Materiality Threshold
8. Commodities contracts:
 - (a) Futures and forward contracts
 - (b) Option contracts (e.g., options on individual commodities and commodities indexes):
 - (i) Sold option contracts
 - (ii) Purchased option contracts
9. Securities contracts:
 - (a) Futures and forward contracts (e.g., stock index contracts)

- (b) Option contracts (e.g., options on individual securities and securities indexes):
 - (i) Sold option contracts
 - (ii) Purchased option contracts
10. Foreign exchange contracts:
 - (a) Commitments to purchase foreign currencies and U.S. dollar exchange (include futures and forwards)
 - (b) Option contracts (e.g., options on foreign currencies)
 - (i) Written option contracts
 - (ii) Purchased option contracts
11. Loan commitments and letters of credit (report only unused portions of commitments that are fee paid or otherwise legally binding):
 - (a) Revolving, open-end loans secured by 1-4 family residential properties, e.g., home equity lines
 - (b) Commercial real estate, construction and land development:
 - (i) Commitments to fund loans secured by real estate
 - (ii) Commitments to fund loans not secured by real estate
12. Securities underwriting
13. Other unused commitments
14. Total standby, commercial and similar letters of credit or guarantees
15. Securities borrowed
16. Securities lent
17. Assets sold with recourse:
 - (a) 1-4 family residential mortgages
 - (b) Other loans
 - (c) Other assets
18. Participations in acceptances:
 - (a) Conveyed to others by the Material Associated Person
 - (b) Acquired by the Material Associated Person
19. Other off-balance sheet items (list below each component of this item that exceeds the Materiality Threshold)
20. Information about concentration of credit risk of all financial instruments. See the requirements of FASB Statement 105, paragraph 20.
21. Summary of delta or similar analysis (if available).

Funding Sources (Include Scheduled Maturity Date)

1. Short-term borrowings
 - (a) Commercial paper
 - (b) Bank loans-secured
 - (c) Bank loans-unsecured
 - (d) Other
 - (e) Total
2. Repurchase agreements
3. Long-term debt
4. Committed lines of credit
5. Amounts borrowed under credit lines
6. Credit ratings for commercial paper
 - (a) Standard & Poor's Corporation
 - (b) Moody's Investor Service
 - (c) Other Nationally Recognized Statistical Rating Organization

Real Estate

1. Real estate loans:
 - (a) Construction and land development
 - (b) Secured by farmland
 - (c) Secured by 1-4 family residential properties

- (d) Secured by multi-family (5 or more) residential properties
 - (e) Secured by non-farm non-residential properties
 - (f) Commercial and industrial
 - (g) Lease financing
 - (h) Other
2. Real estate investments:
- (a) Construction and land development
 - (b) Farmland
 - (c) One to four family residential properties
 - (d) Multi-family (5 or more) residential properties

- (e) Non-farm non-residential properties
 - (f) Commercial and industrial
 - (g) Lease financing
 - (h) Other
3. Provide a separate listing of the above information for each geographic region (e.g., northeast, southwest, etc.) and by year the loan or investment was made, with all investments or loans entered into or made before 1986 aggregated into a single category.

Investments in Associated Companies

1. Equity investments in associated companies
2. Non-equity investments in and receivables due from associated companies:
 - (a) Loans, advances, notes, bonds and debentures
 - (b) Other receivables

By the Commission.
 Dated: August 30, 1991.
 Margaret H. McFarland,
 Deputy Secretary.
 [FR Doc. 91-21323 Filed 9-5-91; 8:45 am].
 BILLING CODE 8010-01-M

Securities Exchange Act of 1934
 Release No. 29636 / August 30, 1991

An order has been issued granting the application of The Continuum Company, to strike from listing and registration its Common Stock, \$.10 Par Value, on the American Stock Exchange, Inc.

Securities Exchange Act of 1934
 Release No. 29637 / August 30, 1991

An order has been issued granting the application of the Philadelphia Stock Exchange, Inc. for unlisted trading privileges in the common stock of the following issues which are listed and registered on one or more other national securities exchange and are reported in the consolidated transaction reporting system:

- Smart & Final, Inc.
 Common Stock, \$0.01 Par Value (File No. 7-7142)
- Singer Company N.V.
 Common Stock, \$0.01 Par Value (File No. 7-7143)
- General Motors Corporation
 Mandatory Redeemable Preference Stock, Series A \$0.10 Par Value (File No. 7-7144)
- MGIC Investment Corporation
 Common Stock, \$1.00 Par Value (File No. 7-7145)

[Release No. 34-29636; File No. SR-NASD-90-18]
 56 FR 44108 09/06/91
**Self-Regulatory Organizations;
 National Association of Securities
 Dealers, Inc.; Order Approving
 Proposed Rule Change Relating to the
 Criteria For Initial and Continued
 Inclusion on the NASDAQ System**

August 30, 1991.
 The National Association of Securities Dealers, Inc. ("NASD" or "Association") filed a proposed rule change on April 9, 1990, pursuant to section 19(b)(1) of the