

Beacon (NDB) to serve Runway 15. Controlled airspace extending upward from 700 to 1200 feet above ground level (AGL) is needed for aircraft executing the approach. The intended effect of this proposal is to provide segregation of aircraft using instrument approach procedures in instrument conditions from other aircraft operating in visual weather conditions.

DATES: Comments must be received on or before February 29, 1996.

ADDRESSES: Send comments on the proposal in triplicate to: Federal Aviation Administration, Office of the Assistant Chief Counsel, AGL-7, Rules Docket No. 95-AGL-20, 2300 East Devon Avenue, Des Plaines, Illinois 60018.

The official docket may be examined in the Office of the Assistant Chief Counsel, Federal Aviation Administration, 2300 East Devon Avenue, Des Plaines, Illinois. An informal docket may also be examined during normal business hours at the Air Traffic Division, System Management Branch, Federal Aviation Administration, 2300 East Devon Avenue, Des Plaines, Illinois.

FOR FURTHER INFORMATION CONTACT: Eleanor J. Williams, Air Traffic Division, System Management Branch, AGL-530, Federal Aviation Administration, 2300 East Devon Avenue, Des Plaines, Illinois 60018, telephone (708) 294-7568.

SUPPLEMENTARY INFORMATION:

Comments Invited

Interested parties are invited to participate in this proposed rulemaking by submitting such written data, views, or arguments as they may desire. Comments that provide the factual basis supporting the views and suggestions presented are particularly helpful in developing reasoned regulatory decisions on the proposal. Comments are specifically invited on the overall regulatory, aeronautical, economic, environmental, and energy-related aspects of the proposal.

Communications should identify the airspace docket number and be submitted in triplicate to the address listed above. Commenters wishing the FAA to acknowledge receipt of their comments on this notice must submit with those comments a self-addressed, stamped postcard on which the following statement is made: "Comments to Airspace Docket No. 95-AGL-20." The postcard will be date/time stamped and returned to the commenter. All communications received on or before the specified closing date for comments will be considered before taking action on the

proposed rule. The proposal contained in this notice may be changed in light of comments received. All comments submitted will be available for examination in the Rules Docket, FAA, Great Lakes Region, Office of the Assistant Chief Counsel, 2300 East Devon Avenue, Des Plaines, Illinois, both before and after the closing date for comments. A report summarizing each substantive public contact with FAA personnel concerned with this rulemaking will be filed in the docket.

Availability of NPRM's

Any person may obtain a copy of the Notice of Proposed Rulemaking (NPRM) by submitting a request to the Federal Aviation Administration, Office of Public Affairs, Attention: Public Inquiry Center, APA-230, 800 Independence Avenue, S.W., Washington, DC 20591, or by calling (202) 267-3484. Communications must identify the notice number of this NPRM. Persons interested in being placed on a mailing list for future NPRM's should also request a copy of Advisory Circular No. 11-2A, which describes the application procedure.

The Proposal

The FAA is considering an amendment to part 71 of the Federal Aviation Regulations (14 CFR part 71) to establish Class E5 airspace at Bigfork Municipal Airport, Bigfork, MN, to accommodate a Nondirectional Radio Beacon (NDB) to serve Runway 15. Controlled airspace extending upward from 700 to 1200 feet AGL is needed to contain aircraft executing the approach. The intended effect of this action is to provide segregation of aircraft using instrument approach procedures in instrument conditions from other aircraft operating in visual weather conditions. The area would be depicted on appropriate aeronautical charts thereby enabling pilots to circumnavigate the area or otherwise comply with IFR procedures. Class E airspace designations for airspace areas extending upward from 700 feet or more above the surface of the earth are published in paragraph 6005 of FAA Order 7400.9C dated August 17, 1995, and effective September 16, 1995, which is incorporated by reference in 14 CFR 71.1. The Class E airspace designation listed in this document would be published subsequently in the Order.

The FAA has determined that this proposed regulation only involves an established body of technical regulations for which frequent and routine amendments are necessary to keep them operationally current. Therefore this, proposed regulation—(1)

is not a "significant regulatory action" under Executive Order 12866; (2) is not a "significant rule" under DOT Regulatory Policies and Procedures (44 FR 11034; February 26, 1979); and (3) does not warrant preparation of a Regulatory Evaluation as the anticipated impact is so minimal. Since this is a routine matter that will only affect air traffic procedures and air navigation, it is certified that this proposed rule will not have a significant economic impact on a substantial number of small entities under the criteria of the Regulatory Flexibility Act.

List of Subjects in 14 CFR Part 71

Airspace, Incorporation by reference, Navigation (air).

The Proposed Amendment

Accordingly, pursuant to the authority delegated to me, the Federal Aviation Administration proposes to amend part 71 of the Federal Aviation Regulations (14 CFR part 71) as follows:

PART 71—[AMENDED]

1. The authority citation for part 71 continues to read as follows:

Authority: 49 U.S.C. 106(g), 40103, 40113, 40120; E.O. 10854, 24 FR 9565, 3 CFR, 1959-1963 Comp., p. 389; 14 CFR 11.69.

§ 71.1 [Amended]

2. The incorporation by reference in 14 CFR 71.1 of the Federal Aviation Administration Order 7400.9C, Airspace Designations and Reporting Points, dated August 17, 1995, and effective September 16, 1995, is amended as follows:

Paragraph 6005 The Class E airspace areas extending upward from 700 feet or more above the surface of the earth.

* * * * *

AGL MN E5 Bigfork, MN [New]

Bigfork Municipal Airport, MN
(lat. 47°46'44.7" N, long. 93°39'00.6" W)

That airspace extending upward from 700 feet above the surface within a 7-mile radius of the Bigfork Municipal Airport.

* * * * *

Issued in Des Plaines, Illinois on November 22, 1996.

Maureen Woods,

Acting Manager, Air Traffic Division.

FR Doc. 95-30370 Filed 12-12-95; 8:45 am]

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

AGENCY: Commodity Futures Trading Commission.

ACTION: Proposed rules.

SUMMARY: The Commodity Futures Trading Commission (Commission) proposes to amend: (1) Rules 1.17(a)(1)(i) and (ii) to (a) increase the minimum required dollar amount of adjusted net capital for futures commission merchants (FCMs) from \$50,000 to \$250,000, (b) increase the minimum required dollar amount of adjusted net capital for introducing brokers (IBs) from \$20,000 to \$30,000, and (c) make the amount of adjusted net capital required by a registered futures association for its member FCMs and IBs an element of the Commission's minimum financial requirements for FCMs and IBs; (2) Rule 1.17(h)(2)(vii) with respect to the procedure to obtain approval for prepayment of subordinated debt; and (3) Rule 1.58, which governs gross collection of exchange-set margins for omnibus accounts, to make it applicable to omnibus accounts carried by FCMs for foreign brokers. The Commission believes that these amendments will conform the Commission's rules with those of industry self-regulatory organizations (SROs) and therefore should not require changes in the operations of most firms.

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

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

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

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

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

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

¹ 7 U.S.C. 6d(2) (1994).

² 17 CFR 30.7 (1995).

³ Commission Rule 170.15 mandates that each person required to register as an FCM become and remain a member of a futures association which provides for the membership therein of such FCM unless there is no registered futures association. National Futures Association (NFA) is the only registered futures association. It has an FCM membership category and virtually all FCMs are NFA members. However, there are approximately 90 firms registered as FCMs (out of a total of approximately 260) that do not handle customer funds and therefore are not required to register as FCMs. Accordingly, these firms are not required to be NFA members pursuant to Commission Rule 170.15 but almost all of them are NFA members anyway. However, there still are approximately ten registered FCMs that are not members of any SRO and thus have a current minimum dollar adjusted net capital requirement of \$100,000 under Commission Rule 1.17(a)(1)(i)(A). Since such a small number of firms are in this category, for ease of discussion we shall assume that all registered FCMs currently have a minimum dollar requirement of adjusted net capital of \$50,000 under Commission rules.

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

⁵ On November 24, 1992, the SEC also adopted rule amendments to raise its minimum net capital requirement for securities broker-dealers holding customer funds, which had been \$25,000, to \$250,000 in stages. The requirement increased to \$100,000 effective July 1, 1993, \$175,000 effective January 1, 1994 and to the current level of \$250,000 effective July 1, 1994. See 57 FR 56973, 56990 (Dec. 2, 1992); 17 CFR § 240.15c3-1e(a) (1995).

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

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

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

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

The Commission nonetheless believes that raising the required minimum dollar amount of adjusted net capital for FCMs under Commission Rule 1.17 to that required by NFA and CBT for their members is necessary and appropriate for the following reasons. Section 8c(a)(1) of the Act, 7 U.S.C. 12c(a)(1) (1994), authorizes the Commission to discipline a member of an exchange in accordance with the rules of that exchange if the exchange fails to do so. Section 17(l)(1) of the Act, 7 U.S.C. 21(1)(1) (1994), authorizes the Commission to suspend a registered futures association that has failed to enforce compliance with its own rules. However, the Commission does not have the authority to discipline an exchange member for violation of an exchange rule in the absence of the exchange's failure to act, or to enforce compliance with a registered futures association's own rule upon a member thereof. This limitation upon the Commission's enforcement remedies in the context of SRO rules does not, of course, exist in the context of violations of the Act or Commission regulations. Section 6c of the Act, 7 U.S.C. 13a-1 (1994), authorizes the Commission, whenever it appears that a person has engaged, is engaging, or is about to engage in any act or practice constituting a violation of any provision of the Act or any rule or regulation thereunder, to bring an action to enjoin such act or practice, or to enforce compliance with the Act or any rule or regulation thereunder.

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

compliance with what is effectively, for the reasons discussed above, the current minimum adjusted net capital requirement applicable to FCMs with the benefit of all of the remedies available to it under the Act for the enforcement of compliance with any provision of the Act and any rule promulgated thereunder. In addition, this amendment would harmonize the Commission's minimum dollar requirement for FCMs with the prevailing standards established by NFA rules and support the objective of assuring that FCMs have a substantial base of liquid capital from which to meet their obligations to customers, an objective for which an increased requirement appears appropriate given the increase in the amount of funds held by FCMs and the change in the value of the dollar since 1978.

The Commission believes it is necessary to clarify its authority to require the transfer of positions at such time as a firm is no longer in compliance with the NFA rule. The Commission further believes that a base minimum adjusted net capital requirement of \$250,000 is now essential to providing both an adequate stake in doing business in accordance with Commission rules and otherwise to provide a cushion sufficient with applicable haircuts and segregation of customer funds to permit the Commission to act in an emergency. The Commission also believes that the rule amendment is necessary to eliminate any confusion that may have existed as to whether the Commission could take action where an FCM's adjusted net capital is below \$250,000 yet still exceeds \$50,000.

Accordingly, the Commission is proposing to amend Rule 1.17(a)(1)(i)(A) to increase the minimum dollar amount of adjusted net capital for FCMs to \$250,000.⁸ In light of the amount of the proposed increase and the fact that, unlike the situation in 1978, very few FCMs are not members of any SRO and that those few FCMs in that category cannot handle customer funds, the Commission sees no need to maintain a higher dollar amount of required adjusted net capital for an FCM that is not a member of any SRO. In any event,

⁸The Commission believes, for the reasons discussed above, that an increase from \$50,000 to \$250,000 is necessary and that it is unnecessary to phase this in over time as the SEC did in that most firms already meet the NFA requirement. The Commission also notes that when it adopted the current \$50,000 standard in 1978, that was also a five-fold, one-step increase in the existing standard of \$10,000 of working capital originally adopted by the Commission's predecessor agency, the Commodity Exchange Authority, effective March 17, 1969. 34 FR 599 (Jan. 16, 1969).

such FCMs would have an increase in their adjusted net capital requirement from the current \$100,000 to the proposed \$250,000 that would apply to all FCMs.

The Commission further notes that several provisions of the Commission's minimum financial rules for FCMs, as well as one provision of the financial early warning system, contain cross-references to Rule 1.17(a)(1)(i)(A). Certain actions are restricted or required if the specified levels of adjusted net capital, which in all cases exceed 100 percent of the minimum dollar amount, are breached. These include Rule 1.17(e)(1)(i) (restricting the withdrawals of equity capital as well as the following paragraphs of Rule 1.17 concerning subordinated debt: paragraph (h)(2)(vi)(C)(I) (restricting the parties to a secured demand note (SDN) agreement from providing in such agreement that the unpaid principal amount of an SDN can be reduced below a floor amount if the value of collateral securing the SDN declines below the unpaid principal amount); paragraphs (h)(2)(vii)(A)(I) and (B)(I) (restricting prepayments and special prepayments); (h)(2)(viii)(A)(I) (requiring suspension of repayment); (h)(3)(ii)(A) (requiring notice of maturity or accelerated maturity); and (h)(3)(v)(A) (restricting use of temporary subordinations). In addition, Rule 1.12(b)(1) establishes the "early warning" minimum dollar level of adjusted net capital as 150 percent of the minimum dollar requirement, triggering notice and follow-up reporting requirements when an FCM's adjusted net capital is below that level. Even though the Commission is not amending the provisions of Rules 1.12 and 1.17 that cross-reference Rule 1.17(a)(1)(i)(A), the proposed amendment of the latter will have a corresponding impact on the various FCM activities or obligations referred to above.⁹

The Commission held a roundtable on capital on September 18, 1995 where several issues were discussed pertaining to minimum financial requirements. One of the issues discussed was whether the second prong of the current requirement, based upon four percent of the sum of segregated customer funds and the secured amount, should be

⁹For example, equity capital withdrawals from an FCM currently cannot reduce the FCM's adjusted net capital below \$60,000 (120 percent of the minimum amount); if the amendment proposed herein to Rule 1.17(a)(1)(i)(A) were adopted, equity capital withdrawals would not be permitted to reduce the FCM's adjusted net capital below \$300,000. Similarly, the "early warning" level of adjusted net capital would increase from \$75,000 to \$375,000 despite the fact that Rule 1.12(b)(1) itself would not be amended.

amended in an effort to make an FCM's minimum adjusted net capital requirement reflect more closely the risks to an FCM caused by carrying open positions. The Commission may address that issue in a subsequent release following a review of empirical data being developed by the SROs but is not prepared to do so at this time.

B. Minimum Financial Requirements for IBs

Rule 1.17 also requires introducing brokers (IBs)¹⁰ to maintain certain prescribed minimum amounts of adjusted net capital. Pursuant to Rule 1.17(a)(1)(ii), each person registered as an IB must maintain adjusted net capital equal to or in excess of the greater of: (A) \$20,000 (\$40,000 for each person registered as an IB who is not a member of an SRO);¹¹ or, (B) if the IB is also a securities broker-dealer, the amount of net capital required by the SEC.

On October 6, 1992, the Commission approved NFA rule amendments which, among other things, increased the required minimum dollar amount of adjusted net capital for member IBs from \$20,000 to \$30,000. However, the Commission did not at that time amend Commission Rule 1.17(a)(1)(ii)(A) to conform to NFA's rule amendment. The Commission believes that since it is now proposing to raise the minimum dollar amount of required adjusted net capital for FCMs as discussed above, it is appropriate also to propose an increase in the required minimum dollar amount of adjusted net capital for IBs. Accordingly, the Commission is proposing to amend Rule 1.17(a)(1)(ii)(A) to raise the minimum dollar amount of required net capital for a registered IB to \$30,000. For reasons similar to those discussed above concerning FCMs, the Commission would eliminate any higher requirement for an IB that is not a member of an SRO.

¹⁰Section 1a(14) of the Act, 7 U.S.C. 1a(14)(1994), defines an IB as "any person (except an individual who elects to be and is registered as an associated person of [an FCM]) engaged in soliciting or in accepting orders for the purchase or sale of any commodity for future delivery on or subject to the rules of any contract market who does not accept any money, securities or property (or extend credit in lieu thereof) to margin, guarantee, or secure any trades or contracts that result or may result therefrom." Commission Rule 1.3(mm), 17 CFR 1.3(mm) (1995), also includes in the definition of an IB any person required to register as such by virtue of Part 33 of the Commission's rules, 17 CFR Part 33 (1995).

¹¹As is the case with FCMs discussed above, virtually all registered IBs are members of NFA. Any IB that is registered but not an NFA member would be precluded from introducing customer accounts to an FCM and thus could not act as an IB.

This proposed amendment, like the proposal applicable to FCMs, would conform to the Commission's rule to the general industry standard established by NFA. Therefore, there should be essentially no impact on the operations of IBs as a result of this amendment. In any event, the proposed amendment would only affect the minority of IBs who raise their own capital. Those IBs who have entered into guarantee agreements with FCMs would be unaffected by the proposed amendment.¹²

C. Conforming Commission and Registered Futures Association Rules

The Commission also approved NFA rule amendments on October 6, 1992 which provide that a member IB's minimum adjusted net capital requirement, as well as that of a member FCM, can be determined by the number of offices it operates and the number of APs it sponsors.¹³ When NFA presented these provisions to the Commission, NFA stated that the amount of the IB minimum financial requirement should be linked to the size of an IB's operation and that it concluded, after studying several factors related to an IB's business, that the number of offices operated or APs sponsored by an IB were the most relevant factors to be used in a formula establishing an IB's minimum financial requirement. NFA also stated that an FCM's minimum financial requirement should parallel that of an IB in this regard.¹⁴ The

¹² More than two-thirds of IBs enter into guarantee agreements with FCMs in accordance with Commission Rules 1.17(a)(2)(ii) and 1.10(j) in lieu of raising their own capital.

¹³ Section 9 of NFA's Financial Requirements is entitled "Introducing Broker Financial Requirements" and provides as follows:

Each Member IB, except an IB operating pursuant to a guarantee agreement which meets the requirements set forth in CFTC Regulation 1.10(j), must maintain "Adjusted Net Capital" (as defined in Schedule A hereto) equal to or in excess of the greatest of:

- (i) \$30,000; or
- (ii) \$6,000 per office operated by the IB (including the main office); or
- (iii) \$3,000 for each AP sponsored by the IB; or
- (iv) (for securities brokers and dealers), the amount of net capital required by Rule 15c3-1(a) of the Securities and Exchange Commission (17 CFR 240.15c3-1(a)).

The corresponding provision for an FCM with respect to offices and APs is based upon "\$6,000 for each remote location operated (i.e., proprietary branch offices, main office of each guaranteed IB and branch offices of each guaranteed IB); or, \$3,000 for each AP sponsored (including APs sponsored by guaranteed IBs)." Section 1 of NFA's Financial Requirements.

¹⁴ According to discussions with NFA staff, there are currently less than ten FCMs and less than ten IBs whose minimum financial requirement is based upon the number of offices operated or APs sponsored. As of September 30, 1995, of the registered IBs, 1,080 operated pursuant to guarantee

Commission believes that it should incorporate the NFA standards concerning the number of offices or APs sponsored into the minimum financial requirements for FCMs and IBs in Rule 1.17, and eliminate the necessity to amend Rule 1.17 each time NFA amends its minimum financial requirements in order to avoid a recurrence of the current situation where NFA's minimum dollar amount of adjusted net capital for an FCM is \$250,000 and the Commission's minimum is \$50,000. Therefore, the Commission is proposing to redesignate paragraphs (a)(1)(i)(C) and (a)(1)(ii)(B) as paragraphs (a)(1)(i)(D) and (a)(1)(ii)(C), respectively, of Rule 1.17, and to add new paragraphs (a)(1)(i)(C) and (a)(1)(ii)(B) that would provide that "the amount of adjusted net capital required by a registered futures association of which it is a member" is an element of the Commission's minimum financial requirement for FCMs and IBs. The Commission is also proposing conforming amendments to the early warning level of adjusted net capital for FCMs,¹⁵ the restriction on withdrawals of equity capital and the various provisions of Rule 1.17(h) discussed above concerning subordinated debt.¹⁶

II. Prepayment of Subordinated Debt

For purposes of computing net capital, debt covered by "satisfactory subordinated agreements" can be excluded from liabilities.¹⁷ Rule 1.17(h)(2)(vii)(A) generally prohibits any prepayment of subordinated debt for one year following the date upon which the governing subordination agreement became effective. However, Rule 1.17(h)(2)(vii)(B) permits special prepayment of subordinated debt at any time (even during the first year)

agreements with an FCM and 388 were raising their own capital.

¹⁵ See proposed new paragraph (b)(3) of Rule 1.12, which is based upon 150% of the amount of adjusted net capital required by a registered futures association, and is proportional to the other elements of Rule 1.12(b).

¹⁶ See the following proposed new Rule 1.17(e)(1)(iii) and the proposed new paragraphs of Rule 1.17: (h)(2)(vi)(C)(3) (restricting reductions in unpaid principal amount of an SDN); (h)(2)(vii)(A)(3) (restricting prepayments); (h)(2)(vii)(B)(3) (restricting special prepayments); (h)(2)(viii)(A)(3) (requiring suspension of repayment); (h)(3)(ii)(C) (requiring notice of maturity or accelerated maturity); and (h)(3)(v)(C) (restricting use of temporary subordinations). The levels of adjusted net capital set forth in the proposed new paragraphs of Rule 1.17 are 120 percent of the registered futures association's minimum amount, except for the provision concerning special prepayment which would be 200 percent. These percentages correspond to the current levels in those rules that are based upon the minimum dollar amount.

¹⁷ See Commission Rule 1.17(h) for a definition of the term "satisfactory subordination agreement".

provided that, after giving effect thereto, the applicant's or registrant's adjusted net capital does not fall below certain amounts prescribed in the rule, which are approximately one and one-half times the amounts of capital required for a normal prepayment. In addition, no prepayment and no special prepayment may occur unless the registrant has obtained written approval of its designated self-regulatory organization (DSRO), if any, and the Commission.¹⁸

On September 10, 1985, the Commission's Division of Trading and Markets (Division) advised all registered IBs, FCMs and SROs of its intention to recommend to the Commission that Rule 1.17(h)(2)(vii) be changed to require only the DSRO's approval for prepayment of subordinated debt.¹⁹ "The requirement for dual approval has been in effect for approximately seven years", the Division stated, "[d]uring [which] time, the DSROs have gained greater familiarity regarding subordinated debt and * * * have demonstrated * * * an ability to work together in the area of financial surveillance." This change would "make the treatment of prepayment of subordinated debt consistent with the treatment of approval of new subordinated debt or amendments to subordinated agreements."

The Commission is proposing to implement the change contemplated in Interpretative Letter No. 85-17 by amending Rule 1.17(h)(2)(vii) to require submission of a request for approval of prepayment of subordinated debt by a registrant to the DSRO only, if any, or to the Commission in those rare instances where the registrant is not an SRO member. Dual approval by the DSRO and the Commission would be required, however, should the requested prepayment or special prepayment result in a reduction of 20 percent or more of the registrant's adjusted net capital. Therefore, if a firm's subordinated debt amounts to 25 percent of its adjusted net capital and the firm wishes to prepay all of it and simultaneously enter into new subordinated debt arrangements for the same amount, but at a different maturity or interest rate, dual approval would *not* be required since there would be no net effect on the firm's adjusted net capital. Similarly, if a firm wanted to convert subordinated debt to paid-in-capital, dual approval would not be required so

¹⁸ An applicant for registration must obtain prior written approval of NFA.

¹⁹ CFTC Interpretative Letter No. 85-17, [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶22,738 (Sept. 10, 1985).

long as such conversion did not result in a reduction of 20 percent or more of the firm's adjusted net capital.

III. Gross Collection of Exchange-Set Margins

Pursuant to Commission Rule 1.58, each FCM which carries a commodity futures or commodity option position for another FCM on an omnibus basis must collect, and each FCM for which an omnibus account is being carried must deposit, initial and maintenance margin on each position reported in accordance with Commission Rule 17.04 at a level no less than that established for customer accounts by the rules of the applicable contract market. Rule 1.58 was proposed in 1981²⁰ following the bankruptcy of three FCMs who cleared trades solely by means of omnibus accounts. The Commission was concerned that customer funds were "being held by firms that, in comparison to clearing FCMs, generally [had] less capital and [were] less equipped to handle the volatility of the commodity markets".²¹ It is also the case, as demonstrated during the collapse of Barings PLC, that net margining of an omnibus account can mask risk to the clearing member. Thus, the primary purposes of Rule 1.58 were to "strengthen the industry and enhance customer protection by moving segregated funds into the normally better-capitalized hands of a clearing member" and to provide the Commission and the SROs with better information with respect to omnibus accounts.²²

As originally adopted and currently, Rule 1.58 does not apply to omnibus accounts carried by FCMs on behalf of foreign brokers.²³ On November 16, 1988, the Division issued Financial and Segregation Interpretation No. 12 which, among other things, requires FCMs to obtain an agreement from customers who desire to have funds held offshore whereby such customers authorize the subordination of their claims attributable to funds held offshore to the claims of other customers should the FCM be placed in bankruptcy or receivership. Although the Commission is in the process of reviewing this Interpretation from the perspective of certain foreign currency deposits in light of the provisions for settlement of certain contracts traded on U.S. contract markets by means of foreign currency, certain statements made relative to

foreign location risk remain relevant today. For example, in support of this Interpretation, the Commission expressed its concern that "in the event of an FCM insolvency, deposits maintained at a foreign depository might not be handled or distributed in accordance with United States bankruptcy law" and that "both the size of the pool of funds available for distribution to customers and the size of individual claims against that pool may vary from day-to-day." The Commission further stated that "to the extent foreign domiciled customers deposit [U.S.] dollars in connection with United States futures or options, such funds should be held in the United States" because "the Commission perceives no administrative necessity for FCMs and customers to incur the location risks attendant to holding such dollar deposits overseas".²⁴ Likewise, the Commission is concerned that margin deposits maintained by a foreign broker at a foreign depository might become unavailable in the event of a bankruptcy of the clearing FCM due to differences in bankruptcy law among jurisdictions and might be exposed to currency fluctuations during the pendency of the bankruptcy. In addition, the Commission has observed that in times of turbulent markets, such as occurred in October 1987 and October 1989, accounts in the names of owners with foreign addresses had greater difficulty meeting margin calls than did domestic accounts, undoubtedly to some extent due to time zone differences and currency conversion logistics.²⁵ In this context, the Commission has recognized that foreign brokers' omnibus accounts carried by clearing FCMs can have a substantial impact on the financial condition of clearing FCMs. Further, as a result of the collapse of Barings PLC in February 1995, the Commission's concern has been heightened with respect to FCMs having a clear view of the exposures in omnibus accounts and the ability to assure proper handling and segregation of customer funds.

In view of the increasing internationalization of the financial markets, and in particular the increasing use of foreign omnibus accounts, the Commission believes that foreign broker omnibus accounts should be treated in

the same manner as omnibus accounts carried for domestic FCMs. Thus, FCMs carrying foreign broker omnibus accounts would hold a higher level of funds, have less capital exposure and be better able to transfer positions from such accounts in the event of a financial disruption. Accordingly, the Commission is proposing to expand the application of Rule 1.58 to include foreign brokers' omnibus accounts carried by FCMs. As is the case with the proposed amendments to Rule 1.17 concerning the minimum amount of adjusted net capital for FCMs and IBs, the Commission is essentially proposing to conform its rule relating to collection of margins for omnibus accounts to the industry practice since, as a result of staff recommendations in rule enforcement reviews and SRO rule changes, all active U.S. contract markets other than the New York Cotton Exchange and the Philadelphia Board of Trade require that FCMs collect margin for omnibus accounts of foreign brokers as well as other domestic FCMs on a gross basis.

IV. Other Matters

As noted above, the Commission held a roundtable on capital issues on September 18, 1995, during which several matters were discussed. Although the Commission is not presenting any specific rule proposals at this time related to issues discussed at the roundtable, the Commission will be seeking additional information concerning certain of the issues discussed with a view towards possible additional rule amendments. These issues would include greater harmonization of the CFTC/SEC financial requirements in several areas such as reporting requirements and cycles, early warning requirements,²⁶ risk assessment data elements and the debt-equity ratio requirements with respect to a firm's capital.²⁷ The

²⁶The Commission has proposed amendments to its Rule 1.12 to: (1) make paragraph (g), which requires the reporting of certain reductions in adjusted net capital, applicable to all FCMs, rather than just those FCMs subject to the risk assessment reporting requirements of Rule 1.15; (2) require reporting of a margin call that exceeds an FCM's excess adjusted net capital which remains unanswered by the close of business on the day following the issuance of the call; and (3) require reporting by an FCM whenever its excess adjusted net capital is less than six percent of the maintenance margin required to support proprietary and noncustomer positions carried by the FCM. 59 FR 66822 (Dec. 28, 1994).

²⁷SEC Rule 15c3-1(d) (17 CFR 240.15c3-1(d)) (1995) requires that at least 30 percent of all of a broker-dealer's net capital consist of equity capital. See Report of the Technical Committee of IOSCO, "Capital Requirements for Multinational Securities Firms," XV Annual Conference of the International Organization of Securities Commissions (IOSCO),

²⁴ See 53 FR 46911 (Nov. 21, 1988), reprinted in 1 Comm. Fut. L. Rep. (CCH) ¶ 7122.

²⁵ See Final CFTC Staff Report, *Stock Index Futures and Cash Market Activity—October 1987*, at pp. 192-193 (Jan. 1988) (reprinted in *Comm. Fut. L. Rep. (CCH), Special Report No. 321, Feb. 5, 1988*) and *Commodity Futures Trading Commission, Division of Economic Analysis, Report on Stock Index Futures and Cash Market Activity During October 1989 to the U.S. Commodity Futures Trading Commission*, at p. 143 (May 1990).

²⁰ 46 FR 62864 (Dec. 29, 1981).

²¹ Id.

²² 47 FR 21026 (May 17, 1982).

²³ Neither the proposing release nor the adopting release for Rule 1.58 discuss omnibus accounts carried on behalf of foreign brokers.

Commission is also considering a rethinking of the no-action relief provided to an FCM by the Division with respect to the short options value charge,²⁸ and the appropriateness of a concentration charge. Separately, the Commission has discussed with the Joint Audit Committee the data necessary to evaluate any proposals for a "risk-based" standard as a component of the minimum adjusted net capital requirements. Although the Commission has no specific proposals in any of these areas at this time, it nonetheless invites commenters to address these matters if they so choose.

V. Related Matters

A. Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA), 5 U.S.C. 601 et seq., requires that agencies, in proposing rules, consider the impact of those rules on small businesses. The rule amendments proposed herein would affect FCMs and independent IBs. The Commission has previously determined that, based upon the fiduciary nature of FCM/customer relationships, as well as the requirement that FCMs meet minimum financial requirements, FCMs should be excluded from the definition of small entity.²⁹

With respect to IBs, the Commission stated that it is appropriate to evaluate within the context of a particular rule proposal whether some or all IBs should be considered to be small entities and, if so, to analyze the economic impact on such entities at that time.³⁰ The proposed amendment to Rule 1.17(h)(2)(vii) would generally reduce the burden associated with the procedure to obtain approval for permissive prepayment of subordinated debt. Accordingly, that amendment should impose no additional

Santiago, Chile 1990. The general international standard in this connection, as recommended by Working Party No. 3 of the Technical Committee of IOSCO, would also apply the debt-equity requirement to all of a firm's capital. Although the Commission originally proposed a debt-equity requirement for an FCM that would have been similar to that of a broker-dealer under SEC rules (see 42 FR 27166, 27177 (May 26, 1977)), in response to comments that "it would be inappropriate to penalize a firm that maintains capital in the form of satisfactory subordination agreements, which is in excess of the minimum required by regulations", the Commission revised the required debt-equity total to which the 30 percent equity capital requirement applies to mean total capital less the excess of the FCM's adjusted net capital, *i.e.*, only the required minimum adjusted net capital. See 43 FR 39956, 39965, 39976 (Sept. 8, 1978).

²⁸ Commission Rule 1.17(c)(5)(iii), 17 CFR 1.17(c)(5)(iii) (1995); CFTC Interpretative Letter 95-65, [Current Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,495 (July 26, 1995).

²⁹ See 47 FR 18618, 18619 (Apr. 30, 1982).

³⁰ See 48 FR 35248, 35275-78 (Aug. 3, 1983).

requirements on an independent IB. In addition, the proposed amendment to the minimum adjusted net capital requirement for an IB would conform the Commission's requirement to that of the NFA and therefore there should be no impact on an IB's financial operations. Thus, if adopted, these proposals would not have a significant economic impact on a substantial number of IBs. Therefore, pursuant to Section 3(a) of the RFA, 5 U.S.C. 605(b), the Chairman certifies that these proposed rule amendments will not have a significant economic impact on a substantial number of small entities.

B. Paperwork Reduction Act

The Paperwork Reduction Act of 1990, (PRA) 44 U.S.C. 3501 et seq., imposes certain requirements on Federal agencies (including the Commission) in connection with their conducting or sponsoring any collection of information as defined by the PRA. While the amendments proposed herein have no burden,³¹ Rules 1.12, 1.17 and 1.58 are parts of groups of rules with the following burdens.

The burden associated with the collection required by Rules 1.12 and 1.17 (3038-0024), including these proposed amendments, is as follows:

Average Burden Hours Per Response:
1.50.

Number of FCM Respondents: 165.00.

Number of IB Respondents: 62.00.

Frequency of Response: 1.00.

The burden associated with the collection required by Rule 1.58 (3038-0026), including these proposed amendments, is as follows:

A. Reporting

Average Burden Hours Per Response:
0.04.

Number of Respondents: 100.00.

Frequency of Response: 50.00.

B. Recordkeeping

Average Burden Hours Per Response:
1.00.

Number of Respondents: 300.00.

Frequency of Response: 1.00.

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

³¹ The proposed increase in the dollar amount of minimum adjusted net capital for an FCM and an IB would necessitate only a change in line item 23E of the Statement of the Computation of Minimum Capital Requirements on Form 1-FR-FCM and in line item 15 of that Statement on Form 1-FR-IB.

List of Subjects in 17 CFR Part 1

Commodity futures, minimum financial requirements.

In consideration of the foregoing and pursuant to the authority contained in the Commodity Exchange Act and, in particular, Sections 4f, 4g and 8a(5) thereof, 7 U.S.C. 6f, 6g and 12a(5), the Commission hereby proposes to amend Chapter I of Title 17 of the Code of Federal Regulations as follows:

PART 1—GENERAL REGULATIONS UNDER THE COMMODITY EXCHANGE ACT

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

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

2. Section 1.12 is amended by removing the word "or" at the end of paragraph (b)(2), by redesignating paragraph (b)(3) as paragraph (b)(4), and by adding a new paragraph (b)(3) to read as follows:

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

* * * * *

(b) * * *

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

* * * * *

3. Section 1.17 is amended as follows:

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

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

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

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

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

3.6. By removing the word "or" at the end of paragraph (h)(2)(viii)(A)(2), by redesignating paragraph (h)(2)(viii)(A)(3) as paragraph

(h)(2)(viii)(A)(4), and by adding a new paragraph (h)(2)(viii)(A)(3);

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

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

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

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

(A) \$250,000;

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

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

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

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

(A) \$30,000;

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

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

* * * * *

(e) * * *

(1) * * *

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

* * * * *

(h) * * *

(2) * * *

(vi) * * *

(C) * * *

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

* * * * *

(vii) * * *

(A) * * *

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

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

(B) * * *

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

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

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

(viii) * * *

(A) * * *

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

* * * * *

(3) * * *

(ii) * * *

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

* * * * *

(v) * * *

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

* * * * *

4. Section 1.58 is revised to read as follows:

§ 1.58 Gross collection of exchange-set margins.

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

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

Issued in Washington, D.C. on December 7, 1995 by the Commission.

Jean A. Webb,

Secretary of the Commission.

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DEPARTMENT OF THE INTERIOR

Minerals Management Service

30 CFR Parts 202, 206, and 211

RIN 1010-AC02

Amendments to Gas Valuation Regulations for Federal Leases

AGENCY: Minerals Management Service, Interior.