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United States General Accounting Office
Washington, DC 20548

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June 25, 2004

The Honorable Richard C. Shelby
Chairman
The Honorable Paul S. Sarbanes
Ranking Minority Member
Committee on Banking, Housing, and Urban Affairs
United States Senate

The Honorable Michael G. Oxley
Chairman
The Honorable Barney Frank
Ranking Minority Member
Committee on Financial Services
House of Representatives

Subject: *Securities and Exchange Commission: Alternative Net Capital Requirements for Broker-Dealers That Are Part of Consolidated Supervised Entities*

Pursuant to section 801(a)(2)(A) of title 5, United States Code, this is our report on a major rule promulgated by the Securities and Exchange Commission (Commission), entitled "Alternative Net Capital Requirements for Broker-Dealers That Are Part of Consolidated Supervised Entities" (RIN: 3235-AI96). We received the rule on June 9, 2004. It was published in the Federal Register as a final rule on June 21, 2004. 69 Fed. Reg. 34428.

The final rule establishes a voluntary alternative method for computing net capital for certain broker-dealers. Under the rule, a broker-dealer that maintains certain minimum levels for tentative net capital and net capital may apply for a conditional exemption from the application of the standard net capital calculation. As a condition to granting the exemption, the broker-dealer's ultimate holding company must consent to group-wide Commission supervision related to the financial stability of the broker-dealer.

Enclosed is our assessment of the Commission's compliance with the procedural steps required by section 801(a)(1)(B)(i) through (iv) of title 5 with respect to the rule. Our review indicates that the Commission complied with the applicable requirements.

If you have any questions about this report, please contact James W. Vickers, Assistant General Counsel, at (202) 512-8210. The official responsible for GAO evaluation work relating to the subject matter of the rule is Thomas McCool, Managing Director, Financial Markets and Community Investment. Mr. McCool can be reached at (202) 512-8678.

signed

Kathleen E. Wannisky
Managing Associate General Counsel

Enclosure

cc: Jill M. Peterson
Assistant Secretary
Securities and Exchange Commission

ANALYSIS UNDER 5 U.S.C. § 801(a)(1)(B)(i)-(iv) OF A MAJOR RULE
ISSUED BY THE
SECURITIES AND EXCHANGE COMMISSION
ENTITLED
"ALTERNATIVE NET CAPITAL REQUIREMENTS FOR
BROKER-DEALERS THAT ARE PART OF
CONSOLIDATED SUPERVISED ENTITIES"
(RIN: 3235-AI96)

(i) Cost-benefit analysis

The Commission estimates that approximately 11 broker-dealers will elect to calculate their capital under the amendments in the final rule. It is estimated that it will cost the broker-dealers an average of approximately \$8 million each to modify their information technology systems to meet the rule's requirements, for a total cost of \$88 million.

For the five broker-dealers the Commission expects to apply under the rule that do not have an ultimate holding company that has a principal regulator, the Commission estimates that not being required to form and maintain a sub-holding company in the European Union as a result of Commission group-wide supervision will save those firms approximately \$8 million each for a total savings of \$40 million.

The broker-dealers taking advantage of the alternative capital computation will have lower deductions from net capital for market and credit risk. The Commission estimates that the firms could reallocate that capital to fund business activities for which the rate of return would be approximately 20 basis points (0.2 percent) higher. The total benefit is expected to be approximately \$26 million.

(ii) Agency actions relevant to the Regulatory Flexibility Act, 5 U.S.C. §§ 603-605, 607, and 609

The Commission has certified that the final rule will not have a significant economic impact on a substantial number of small entities.

(iii) Agency actions relevant to sections 202-205 of the Unfunded Mandates Reform Act of 1995, 2 U.S.C. §§ 1532-1535

As an independent regulatory agency, the Commission is not subject to title II of the Unfunded Mandates Reform Act of 1995.

(iv) Other relevant information or requirements under acts and executive orders

Administrative Procedure Act, 5 U.S.C. §§ 551 et seq.

The final rule was promulgated using the notice and comment procedures found at 5 U.S.C. 553. On November 6, 2003, the SEC published a Notice of Proposed Rulemaking in the Federal Register. 68 Fed. Reg. 62872. In response, the Commission received 20 comments, which are discussed in the preamble to the final rule.

Paperwork Reduction Act, 44 U.S.C. §§ 3501-3520

The final rule contains information collections that are subject to review by the Office of Management and Budget (OMB) under the Paperwork Review Act. OMB has approved the information collections. The titles and OMB control numbers for the collections are: (1) Net capital requirements for brokers or dealers, OMB No. 3235-0200; (2) Rule 15c3-4, Internal risk management control systems for certain brokers or dealers, OMB No. 3235-0497; (3) Rule 17a-5, Reports to be made by certain brokers and dealers, OMB No. 3235-0123; (4) Rule 17a-11, Notification procedures for brokers and dealers, OMB No. 3235-0085; (5) Rule 17h-1T, Risk assessment recordkeeping requirements for associated persons of brokers and dealers, OMB No. 3235-0410; and (6) Rule 17h-2T, Risk assessment reporting requirements for brokers and dealers, OMB No. 3235-0410.

Statutory authorization for the rule

The final rule is promulgated under the authority found in 15 U.S.C. 77s, 77o, 77sss, 78d, 78d-1, 78d-2, 78w, 78ll(d), 78mm, 79t, 80a-37, 80b-11, and 7202.

Executive Order No. 12866

As the rule is promulgated by an independent regulatory agency, it is not subject to review requirements of the order.