

Rule 8c-1

Supporting Statement

A. Justification

1. Necessity of Information Collection

The Commission adopted Rule 8c-1 (17 CFR 240.8c-1) in 1940 to furnish added protection to customers against losses incurred as a result of the pledging of customers' securities as collateral by members of national securities exchanges and other broker-dealers. Prior to the adoption of the rule, it had not been prohibited under most customer agreements for a broker-dealer to commingle customer securities with its own securities as collateral for loans used by the firm in its business as a broker-dealer or trader for its own account. In addition, it was not prohibited under most customer agreements for a broker-dealer to borrow more on their customers' securities than was owed them by the customers. The risk of loss to a customer whose securities were so used by a broker-dealer that failed was greatly increased. See Securities Exchange Act Release No. 2690 (November 15, 1940).

As adopted, Rule 8c-1 generally prohibits a broker-dealer from using its customers' securities as collateral to finance its own trading, speculating, or underwriting transactions. More specifically, the rule states three main principles: first, that a broker-dealer is prohibited from commingling the securities of different customers as collateral for a loan without the consent of each customer; second, that a broker-dealer cannot commingle customers' securities with its own securities under the same pledge; and third, that a broker-dealer can only pledge its customers' securities to the extent that customers are in debt to the broker-dealer. See Securities Exchange Act Release No. 2690 (November 15, 1940); Securities Exchange Act Release No. 9428 (December 29, 1971).

The Commission is statutorily authorized by Sections 8(a) and (b) of the Securities Exchange Act of 1934 ("Exchange Act") 15 USC 78h, to adopt rules and regulations that prescribe, under certain circumstances, the hypothecation of any securities carried for the account of any customer. Further statutory authority is found in Section 23(a) of the Exchange Act, 15 USC 78w.

2. Purpose of, and Consequences of Not Requiring, the Information Collection

The information required by the rule is necessary for the execution of the Commission's mandate under the Exchange Act to prevent broker-dealers from hypothecating or arranging for the hypothecation of any securities carried for the account of any customer under certain circumstances. In addition, the information required by the rule provides important investor protections.

3. Role of Improved Information Technology and Obstacles to Reducing Burden

The compilation of this information must be done on an individual basis for each potential investor. Thus, improved information technology would not reduce the burden.

4. Efforts to Identify Duplication

Not applicable; although Rule 15c2-1 under the Exchange Act requires similar information, no rule prohibits combining the notices and consents under both Rules 8c-1 and 15c2-1 in the same documents.

5. Effects on Small Entities

The rule requirements are not unduly burdensome on smaller broker-dealers. Moreover, the requirements prescribed by the rule are those that a prudent businessperson would keep in the ordinary course of business.

6. Consequences of Less Frequent Collection

The information is collected as each transaction warrants and therefore there is no way to require less frequent collection without undermining the purposes of the rule.

7. Inconsistencies with Guidelines in 5 CFR 1320.5(d)(2)

The information collection is not conducted in a matter that is inconsistent with 5 CFR 1320.5(d)(2).

8. Consultations Outside the Agency

Before adoption, Commission rules are published for notice and comment.

9. Payment or Gift to Respondents

Not applicable.

10. Assurances of Confidentiality

No assurances of confidentiality are provided in the statute or the rule.

11. Sensitive Questions

Not applicable; no information of a sensitive nature is required under the rule.

12. Estimate of Respondent Reporting Burden

It is difficult to determine a meaningful estimation of the reporting burden on respondents because of the variation of sizes of broker-dealers subject to the rule. The amount of time required to comply with the rule will vary depending on the amount of customer securities hypothecated by the broker-dealer. Commission staff estimates that for each hypothecation, compliance time will take approximately 10 minutes to create and send notice of hypothecation to the pledgee in accordance with the rule and approximately 20 minutes to request and process consents from customers to permit commingling of customer accounts under the same lien.

There are approximately 142 respondents as of year-end 2006 (i.e., broker-dealers that conducted business with the public, filed Part II of the FOCUS Report, did not claim an exemption from the Reserve Formula computation, and reported that they had a bank loan during at least one quarter of the current year) that require an aggregate total of 3,195 hours to comply with the rule. Each of these approximately 142 registered broker-dealers makes an estimated 45 annual responses, for an aggregate total of 6,390 responses per year. Each response takes approximately 0.5 hours to complete. Thus, the total compliance burden per year is 3,195 burden hours (6,390 responses X 0.5 hours).

The staff estimates that the approximate cost per hour is \$56, resulting in a total cost of compliance for the respondents of approximately \$178,920 (3,195 hours @ \$56 per hour).¹

13. Estimate of Total Annualized Cost Burden

Respondents will not incur any capital, start-up, operational, or maintenance costs. In addition, respondents should not need to purchase any services with regard to the reporting requirements.

14. Estimate of Cost to the Federal Government

Not applicable; the broker-dealers maintain the records required by this rule.

¹ The approximate national hourly rate of \$56 is based on the salary information for compliance clerks set forth in the Securities Industry Association's "Report on Office Salaries in the Securities Industry 2006," as modified to account for an 1800-hour work-year and multiplied by 2.93 to account for bonuses, firm size, employee benefits and overhead.

15. Explanation of Changes in Burden

Changes in burden are reflective of the expanded definition of “collection of information” adopted in the 1995 amendments to the Paperwork Reduction Act and are not indicative of changes in the Commission’s administration of this Rule.

16. Information Collections Planned for Statistical Purposes

Not applicable; there is no intention to publish the information for any purpose.

17. Explanation as to Why Expiration Date Will Not be Displayed

Not applicable.

18. Exceptions to Certification

Not applicable.

B. Collection of Information Employing Statistical Methods

The collection of information does not employ statistical methods, nor would the implementation of such methods reduce the burden or improve accuracy of results.