

## Statement

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# Statement on Proposed Amendments to the Customer Protection Rule



**Commissioner Caroline A. Crenshaw**

**July 12, 2023**

Thank you, Chair Gensler. Since its adoption over 50 years ago, the customer protection rule has been a cornerstone of our broker-dealer regulatory regime.<sup>[1]</sup> The rule protects customer funds and securities by obligating firms to maintain custody of their customers' securities, safeguard customer cash by segregating it from their proprietary business activities, and return the assets promptly to customers upon request. Together with the Securities Investor Protection Act, or SIPA, passed two years earlier, the customer protection rule is designed to ensure that if a broker-dealer fails financially, its customers' securities and cash will be readily available to be returned to those customers.<sup>[2]</sup> If the broker-dealer moves to liquidation, SIPA and the customer protection rule help ensure that customer securities and cash are distributed to customers ahead of other creditors.

These investor protections are part of what distinguishes the regulated securities markets from unregulated and non-compliant markets that lack these important safeguards. For example, if a non-compliant or unregulated market entity fails, its customers' assets and cash may not be subject to SIPA or the customer protection rule. Customer securities and cash may be intermingled with other assets, and in the event of a liquidation, customers might be treated as unsecured creditors, waiting in line behind other, more senior creditors.

The amendments we are proposing today would strengthen the customer protection rule by helping to ensure that broker-dealers maintain sufficient funds to reimburse their customers, as well as other broker-dealers who may have accounts for their proprietary securities and cash ("PAB account holders").<sup>[3]</sup> Currently, Rule 15c3-3 requires a carrying broker-dealer to take two primary steps to safeguard customer assets. The first is that the broker-dealer must maintain physical possession or control over customers' fully paid and excess margin securities. The second is that the broker-dealer must maintain a reserve of funds or qualified securities in an account at a bank that is at least equal in value to the net cash owed to customers.

The amount of net cash owed to customers and PAB account holders is computed weekly as of the close of the last business day of the week. However, as my colleagues have explained, the value of the net cash owed may change daily. This creates the possibility of a significant mismatch between the customer or PAB reserve bank account balances and actual net cash owed.<sup>[4]</sup> As the economic analysis shows, that mismatch can equal hundreds of millions of dollars or even several billion dollars.<sup>[5]</sup> And in the event that a broker-dealer with a large mismatch needs to be liquidated, it could result in the delayed reimbursement of customer securities and cash, and even substantial losses if the customer claims cannot be satisfied.

To address this risk, the proposed amendments would require carrying broker-dealers with large amounts of cash owed to customer and PAB account holders to perform the necessary computations and make any required deposits into their respective customer and PAB reserve bank accounts on a daily, rather than weekly basis.<sup>[6]</sup> Many large broker-dealers already do this on a voluntary basis – however, a significant number do not.<sup>[7]</sup> By requiring broker-dealers to more dynamically match the net amount of cash owed to customers and PAB account holders with the amount on deposit, the amendments should shorten the amount of time for which a mismatch can exist, and thereby better protect customers and the market.

In my view, this is a common-sense change that, if adopted, should help strengthen this important customer safeguard. I hope commenters will provide their feedback, in particular with respect to the scope of the proposal. For example, should the requirement to perform a daily computation apply to all broker-dealers, not just those with the largest amount of customer credits? Do the thresholds and time periods used to determine eligibility for daily computation make sense? I look forward to reviewing the comments on these and all other issues on which the release solicits feedback.

Finally, I'd like to echo my colleagues in thanking the staff, in particular the staff in the Division of Trading and Markets, the Division of Economic and Risk Analysis, and the Office of the General Counsel. I am deeply appreciative of your hard work on this proposal, and I am pleased to support it.

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[1] See 17 CFR 240.15c3-3.

[2] See 15 U.S.C. 78aaa *et seq.*

[3] Daily Computation of Customer and Broker-Dealer Reserve Requirements under the Broker-Dealer Customer Protection Rule, Release No. 34-97877 (July 12, 2023) (the "Proposal"). Broker-dealers are not within the definition of "customer" for purposes of Rule 15c3-3. See 17 CFR 240.15c3-3(a)(1). The definition of "customer" in SIPA, however, is broader than the definition in Rule 15c3-3 in that the SIPA definition includes broker-dealers. See 15 U.S.C. 78lll(2).

[4] Proposal at 7-8.

[5] Proposal at 57, Tables 2-3.

[6] Proposal at 1.

[7] Proposal at 61.