



## Net Capital and Crypto

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One of the many challenging issues the SEC will need to navigate in developing a workable regulatory framework for crypto assets is how to apply the broker-dealer “Net Capital Rule.”

This seemingly narrow, esoteric topic will likely play a role in shaping crypto market structure under the emerging U.S. framework—even if new registration categories such as “crypto broker” and “crypto dealer” emerge from legislation. This is because many institutions will be interested in the feasibility of using their broker-dealer subsidiaries to trade and provide services in crypto and hold stablecoins.

The treatment of crypto under the Net Capital Rule—a rule that considers both securities and non-securities on a firm’s balance sheet—will affect the economic practicality of any such plans.

### **The Net Capital Rule: Purpose and Mechanics**

The Net Capital Rule (Exchange Act Rule 15c3-1) requires SEC-registered broker-dealers<sup>1</sup> to maintain a prescribed measure of net liquid assets, “net capital,” above thresholds that vary based on the type of firm and its functions.<sup>2</sup> The Net Capital Rule’s purpose is critical to understanding the rule and the policy judgments underlying it. The rule is designed to require a firm to maintain a sufficient liquid asset cushion such that if the firm fails, it can self-liquidate in an orderly manner, including transferring customer assets to another broker-dealer—avoiding the costs and delays of a formal liquidation proceeding.<sup>3</sup>

To calculate its “net capital,” a firm takes its GAAP net worth (assets minus liabilities) and applies various adjustments specified in the rule and SEC staff guidance, ultimately arriving at its net capital.<sup>4</sup> Because the rule is intended to address an exigent liquidation scenario, it only recognizes assets that can be “readily converted into cash”—and so, for instance, real estate and office equipment are subtracted.<sup>5</sup>

When calculating net capital, a firm must also make prescribed risk-based deductions, called “haircuts,” to its proprietary positions in securities and other financial products—e.g., broadly speaking, a 15% haircut for equities that have a “ready market” under the rule,<sup>6</sup> a 100% haircut for securities deemed “non-marketable” under the rule<sup>7</sup> and a 20% haircut for commodities.<sup>8</sup>

### **Application to Crypto**

The little guidance that the SEC has published explicitly addressing the application of the Net Capital Rule to crypto reveals a harsh posture. In its 2024 dealer rulemaking release, the Commission stated that crypto assets that are not securities “would be subject to a 100% deduction when computing net capital.”<sup>9</sup> That release also stated that crypto asset securities “that have a ‘ready market,’ as defined in section (c)(11) of the Net Capital Rule, would likely contribute to net capital, subject to haircuts.”<sup>10</sup>

This latter statement concerning crypto asset securities paints a more positive picture than likely warranted in practice: Currently, the rule—as complemented by SEC staff interpretations—does not recognize any crypto asset or crypto market as having or constituting a “ready market.”<sup>11</sup> Further, crypto asset securities may be subject to a 100% haircut (treated as worthless) under the rule on the basis that they could be considered “non-marketable” under the rule, given the outstanding regulatory questions and impediments concerning the sale and trading of

crypto, and the fact that crypto asset securities do not fit neatly into any regulatory bucket that permits a broker-dealer to treat them as marketable.<sup>12</sup>

Treating crypto as worthless for net capital purposes has important implications for an institution considering using its broker-dealer subsidiary for crypto activities, including holding or transacting in stablecoins and providing liquidity services (to name a few). The Net Capital Rule is a moment-to-moment test. And if crypto does not count towards a firm's net capital, the firm may need to fund its crypto positions with a greater amount of equity and/or qualifying subordinated debt, making the crypto-related activity more costly—and potentially, uneconomical to be conducted from a broker-dealer.

The practical effects of the Net Capital Rule vary on a firm-by-firm basis, given the multi-variable application of the rule. But to take a simplified example, if a firm calculates its net capital based on the rule's "Aggregate Indebtedness" standard, and is required to maintain net capital that exceeds 1/15 of its aggregate indebtedness,<sup>13</sup> unsecured borrowing to fund the firm's crypto holdings would have a disproportionately negative effect on its net capital-to-aggregate indebtedness ratio, as compared to similar borrowing to fund assets that have net capital value.

### **Need for Data-focused SEC Staff Review**

The cost of capital that needs to be allocated to a crypto business from a broker-dealer may cause a firm to limit the activity and/or shift it to another subsidiary—assuming, for crypto asset securities, there is another viable subsidiary that can conduct that activity under the ultimate regulatory framework.

In a February 2025 statement, SEC Commissioner Peirce requested comment on numerous crypto topics, including net capital haircuts and the key net capital concept "readily convertible into cash."<sup>14</sup> This was a constructive first step.

It would also be beneficial for the SEC staff to conduct a data-based public review of the Net Capital Rule's application to crypto. A review of this type should include at least three components.

- *First*, it should address the key issue of whether crypto assets should have net capital value. Assuming that some crypto assets should, the review should discuss possible methodologies for assigning appropriate haircuts for different categories of crypto assets, taking into account relevant legal, market, credit, liquidity and other risks.<sup>15</sup>
- *Second*, the review should set out net capital calculations that apply different potential haircuts for sample portfolios comprised of traditional and crypto assets—e.g., stocks, bonds, Bitcoin, Ethereum, different stablecoins and various other crypto assets.
- *Third*, the review should examine key definitional terms and concepts in the Net Capital Rule and existing SEC staff interpretations as relevant to crypto assets—e.g., the concepts of "readily convertible into cash," "ready market" and "non-marketable." This will help facilitate a dialogue on whether any updates are appropriate.

Given the quantitative, multi-variable and firm-specific application of the Net Capital Rule, a staff review of this type would provide the SEC Commissioners (and Congress) with a clearer, more concrete understanding of how a range of possible policy choices may affect costs and market structure. A staff review would also help increase public understanding and confidence in the decisions the Commission ultimately makes.

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<sup>1</sup> The Net Capital Rule works together with other SEC and FINRA rules and is a foundational component of what are commonly called the broker-dealer “financial responsibility rules.”

<sup>2</sup> Broker-dealers generally choose between two net capital standards. The “Aggregate Indebtedness” standard requires net capital to exceed the greater of (i) 1/15 of the broker-dealer’s aggregate indebtedness, and (ii) a fixed dollar amount that varies by broker-dealer type. The “Alternative Standard” requires net capital to exceed the greater of (i) 2% of aggregate debit items computed in accordance with the Reserve Formula in Exhibit A to Rule 15c3-3, and (ii) \$250,000. See Rule 15c3-1(a).

<sup>3</sup> See, e.g., *Alternative Net Capital Requirements for Broker-Dealers that are Part of Consolidated Supervised Entities*, 69 FR 34428, 34430 (June 21, 2004) (“The principal purposes of Exchange Act Rule 15c3-1 . . . are to protect customers and other market participants from broker-dealer failures and to enable those firms that fall below the minimum net capital requirements to liquidate in an orderly fashion without the need for a formal proceeding or financial assistance from [SIPC].”).

<sup>4</sup> See Rule 15c3-1(c)(2).

<sup>5</sup> See Rule 15c3-1(c)(2)(iv).

<sup>6</sup> See Rule 15c3-1(c)(2)(vi)(J).

<sup>7</sup> See Rule 15c3-1(c)(2)(vii).

<sup>8</sup> See Rule 15c3-1b(a)(3)(ix)(C).

<sup>9</sup> Further Definition of “As a Part of a Regular Business” in the Definition of Dealer and Government Securities Dealer in Connection With Certain Liquidity Providers, 89 FR 14938, 14988 (Feb. 29, 2025).

<sup>10</sup> *Id.*

<sup>11</sup> The term “ready market” is defined in Rule 15c3-1(c)(11) to include a “recognized established securities market in which there exists independent bona fide offers to buy and sell so that a price reasonably related to the last sales price or current bona fide competitive bid and offer quotations can be determined for a particular security almost instantaneously and where payment will be received in settlement of a sale at such price within a relatively short time conforming to trade custom” or, alternatively, “where securities have been accepted as collateral for a loan by a bank as defined in section 3(a)(6) of the Securities Exchange Act of 1934 and where the broker or dealer demonstrates to its Examining Authority that such securities adequately secure such loans” as that term is defined Rule 15c3-1(c)(5). Many of the SEC staff’s interpretations of the Net Capital Rule are available on FINRA’s website at <https://www.finra.org/rules-guidance/guidance/interpretations-financial-operational-rules>.

<sup>12</sup> A security is deemed “non-marketable” under the rule where it “cannot be publicly offered or sold because of statutory, regulatory or contractual arrangements or other restrictions” (conceivably the case for crypto, given the outstanding regulatory questions concerning broker-dealers’ ability to transact in crypto). Rule 15c3-1(c)(2)(vii). See also Interpretation and Guide to Net Capital Computation for Brokers and Dealers, 32 FR 856, 858 (Jan. 25, 1967) (“[T]he Commission held . . . that securities which can be publicly offered or sold by the broker or dealer only after registration under the Securities Act of 1933 or pursuant to some exemption under . . . the Act should be given no value for “net capital” purposes until such securities have been effectively registered or there has been compliance with an appropriate exemption . . .”).

<sup>13</sup> This hypothetical assumes that this figure is greater than the alternative fixed dollar amount applicable to the firm under the Aggregate Indebtedness standard. See Rule 15c3-1(a)(1).

<sup>14</sup> Statement of SEC Commissioner Hester M. Peirce, “There Must Be Some Way Out of Here” (Feb. 21, 2025).

<sup>15</sup> See generally Letter from Chelsea Pizzola, Associate General Counsel, Cumberland, to Crypto Task Force, SEC (Apr. 9, 2025) (stating that a “100% haircut for all non-security crypto assets is insupportable, as it fails to consider market data or otherwise account for the distinct liquidity profiles of varying types of non-security crypto assets.”).

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<https://www.yalejreg.com/nc/net-capital-and-crypto/>