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SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 240 and 242

Release No. 34-74834; File No. S7-06-15

RIN 3235-AL73

Application of Certain Title VII Requirements to Security-Based Swap Transactions Connected with a Non-U.S. Person's Dealing Activity That Are Arranged, Negotiated, or Executed By Personnel Located in a U.S. Branch or Office or in a U.S. Branch or Office of an Agent

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rules

SUMMARY: The Securities and Exchange Commission ("SEC" or "Commission") is publishing for comment proposed amendments and a re-proposed rule to address the application of certain provisions of the Securities Exchange Act of 1934 ("Exchange Act") that were added by Subtitle B of Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act") to cross-border security-based swap activities. The Commission is proposing amendments to Exchange Act rules 3a71-3 and 3a71-5 that would address the application of the de minimis exception to security-based swap transactions connected with a non-U.S. person's security-based swap dealing activity that are arranged, negotiated, or executed by personnel of such person located in a U.S. branch or office, or by personnel of such person's agent, located in a U.S. branch or office. The Commission is also re-proposing Exchange Act rule 3a71-3(c) and proposing certain amendments to Exchange Act rule 3a71-3(a) to address the applicability of external business conduct requirements to the U.S. business and foreign business of registered security-based swap dealers. The Commission also is proposing amendments to

Regulation SBSR to apply the regulatory reporting and public dissemination requirements to transactions that are arranged, negotiated, or executed by personnel of non-U.S. persons, or personnel of such non-U.S. persons' agents, that are located in the United States and to transactions effected by or through a registered broker-dealer (including a registered security-based swap execution facility), along with certain related issues, including requiring registered broker-dealers (including registered security-based swap execution facilities) to report certain transactions that are effected by or through the registered broker-dealer.

DATES: Comments should be received on or before **[insert date 60 days after publication in Federal Register]**.

ADDRESSES: Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (http://www.sec.gov/rules/proposed.shtml); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number S7-06-15 on the subject line; or
- Use the Federal eRulemaking Portal (http://www.regulations.gov). Follow the instructions for submitting comments.

Paper Comments:

- Send paper comments to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number S7-06-15. This file number should be included on the subject line if e-mail is used. To help us process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's

Internet website (http://www.sec.gov/rules/proposed.shtml). Comments are also available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549 on official business days between the hours of 10:00 a.m. and 3:00 p.m. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

Studies, memoranda, or other substantive items may be added by the Commission or staff to the comment file during this rulemaking. A notification of the inclusion in the comment file of any such materials will be made available on the SEC's website. To ensure direct electronic receipt of such notifications, sign up through the "Stay Connected" option at www.sec.gov to receive notifications by e-mail.

FOR FURTHER INFORMATION CONTACT: Carol McGee, Assistant Director, Richard Gabbert, Senior Special Counsel, or Margaret Rubin, Special Counsel, Office of Derivatives Policy, at 202-551-5870, Division of Trading and Markets, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-7010.

SUPPLEMENTARY INFORMATION: The Commission is proposing the following rules under the Exchange Act regarding the application of Subtitle B of Title VII of the Dodd-Frank Act to cross-border activities.

The Commission is proposing to amend the following rules under the Exchange Act: rule 3a71-3 (addressing the cross-border implementation of the de minimis exception to the "security-based swap dealer" definition and the definition of certain terms); rule 3a71-5 (regarding availability of an exception from the dealer de minimis analysis for cleared anonymous transactions that fall within proposed rule 3a71-3(b)(1)(iii)(C)); and Rules 900, 901, 906, 907,

908(a)(1), and 908(b) of Regulation SBSR. The Commission also is re-proposing Exchange Act rule 3a71-3(c) (application of external business conduct requirements).

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I. Background

A. Scope of this Rulemaking

The Commission is proposing to amend certain rules and is re-proposing a rule regarding the application of Title VII of the Dodd-Frank Act[1] ("Title VII") to cross-border security-based swap transactions and persons engaged in those transactions. The proposed amendments include rules regarding the application of the de minimis exception to the dealing activity of non-U.S. persons carried out, in relevant part, by personnel located in the United States,[2] and the application of Regulation SBSR[3] to such transactions and to transactions effected by or through a registered broker-dealer, along with certain related issues. We are also re-proposing a rule regarding the application of external business conduct requirements to the foreign business and U.S. business of registered security-based swap dealers.

Each of these issues was considered in our May 23, 2013 proposal, in which we proposed rules regarding the application of Title VII in the cross-border context more generally.[4] On June

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1 Public Law 111–203, 124 Stat. 1376 (2010). Unless otherwise indicated, references to Title VII in this release are to Subtitle B of Title VII.

2 In this release, unless otherwise noted, we use the terms "personnel located in the United States" or "personnel located in a U.S. branch or office" interchangeably to refer to personnel of the non-U.S. person engaged in security-based swap dealing activity who are located in a U.S. branch or office, or to personnel of an agent of such non-U.S. person who are located in a U.S. branch or office.

3 Regulation SBSR—Reporting and Dissemination of Security-Based Swap Information; Final Rule, Exchange Act Release No. 74244 (February 11, 2015), 80 FR 14563 (March 19, 2015) ("Regulation SBSR Adopting Release"). With these proposed rules and rule amendments, the Commission is not re-opening comment on the rules adopted in Regulation SBSR Adopting Release.

4 See Cross-Border Security-Based Swap Activities; Re-Proposal of Regulation SBSR and Certain Rules and Forms Relating to the Registration of Security-Based Swap Dealers and Major Security-Based Swap Participants, Exchange Act Release No. 69490 (May 1, 2013), 78 FR 30968 (May 23, 2013) ("Cross-Border Proposing Release").

25, 2014, we adopted rules and guidance based on the May 23, 2013 proposal addressing the application of the "security-based swap dealer" and "major security-based swap participant" definitions to cross-border security-based swap activities.[5] In that release, among other things, we adopted rules specifying which cross-border transactions must be included in a person's security-based swap dealer de minimis or major security-based swap participant calculations.[6] We explained, however, that we were not addressing the application of the "security-based swap dealer" definition to "transaction[s] conducted within the United States" because commenters had raised several significant issues related to this requirement of the proposal.[7] We stated that we anticipated soliciting additional public comment on the application of the "security-based swap dealer" definition to transactions between two non-U.S. persons where one or both are conducting dealing activity within the United States.[8]

In this release, we propose amendments to Exchange Act rules 3a71-3 and 3a71-5 that reflect a modified approach to this element of the initial proposal and solicit comment on the proposed amendments and re-proposed rule. The proposed amendments would address the activity of a non-U.S. person in the United States in a way that more closely focuses on where personnel of the non-U.S. person engaged in dealing activity (or on where personnel of its agent) are arranging, negotiating, or executing a security-based swap. The proposed amendments would not require a non-U.S. person engaging in dealing activity to consider the location of its

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5 See Application of "Security-Based Swap Dealer" and "Major-Security-Based Swap Participant" Definitions to Cross-Border Security-Based Swap Activities, Exchange Act Release No. 72472 (June 25, 2014), 79 FR 47278 (August 12, 2014 (republication)) ("Cross-Border Adopting Release"). With these proposed rules and rule amendments the Commission is not re-opening comment on the rules adopted in the Cross-Border Adopting Release.

6 See id. at 47279.

7 See id. at 47279-80.

8 See id. at 47280.

non-U.S.-person counterparty or the counterparty's agent in determining whether the transaction needs to be included in its own de minimis calculation. Instead, the proposed amendments would require a non-U.S. person to include in its de minimis calculation any transaction with another non-U.S. person that is, in connection with its dealing activity, arranged, negotiated, or executed by personnel of the non-U.S. person located in a U.S. branch or office or by personnel of the non-U.S. person's agent located in a U.S. branch or office.

We also are re-proposing rules regarding the application of the external business conduct requirements to the foreign business of registered security-based swap dealers, and we are proposing to amend Regulation SBSR to address the reporting and public dissemination requirements applicable to security-based swap transactions involving non-U.S. persons that engage in relevant activity in the United States and to transactions effected by or through a registered broker-dealer, along with certain related issues.

B. The Dodd-Frank Act

Title VII of the Dodd-Frank Act provides for a comprehensive new regulatory framework for swaps and security-based swaps. Under this framework, the Commodity Futures Trading Commission ("CFTC") regulates "swaps" while the Commission regulates "security-based swaps," and the Commission and CFTC jointly regulate "mixed swaps." The new framework encompasses the registration and comprehensive regulation of security-based swap dealers and major security-based swap participants, as well as requirements related to clearing, trade execution, regulatory reporting, and public dissemination.[9] Security-based swap transactions are

[9] We have proposed a series of rules regarding these matters. See Cross-Border Proposing Release, 78 FR 30972 nn.11-18.

The Dodd-Frank Act further provides that the SEC and CFTC jointly should further define certain terms, including "security-based swap dealer" and "major security-based swap participant." See Dodd-Frank Act section 712(d). Pursuant to that requirement, the SEC and CFTC jointly adopted

largely cross-border in practice,[10] and the various market participants and infrastructures operate in a global market. Dealers and other market participants may transact extensively with counterparties established or located in other jurisdictions and, in doing so, may conduct sales and trading activity in one jurisdiction and book the resulting transactions in another. These market realities and the potential impact that these activities may have on U.S. persons and potentially the U.S. financial system have informed our consideration of these proposed rules.

In developing this proposal, we have consulted and coordinated with the CFTC, the prudential regulators,[11] and foreign regulatory authorities in accordance with the consultation mandate of the Dodd-Frank Act.[12] More generally, as part of our domestic and international efforts, Commission staff has participated in numerous bilateral and multilateral discussions with

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rules to further define those terms. See Further Definition of "Swap Dealer," "Security-Based Swap Dealer," "Major Swap Participant," "Major Security-Based Swap Participant" and "Eligible Contract Participant," Exchange Act Release No. 66868 (April 27, 2012), 77 FR 30596 (May 23, 2012) ("Intermediary Definitions Adopting Release"); see also Cross-Border Proposing Release, 78 FR 30972 n.9 (discussing joint rulemaking to further define various Title VII terms).

[10] See Section II.B.2, infra, regarding the preponderance of cross-border activity in the security-based swap market.

[11] The term "prudential regulator" is defined in section 1a(39) of the CEA, 7 U.S.C. 1a(39), and that definition is incorporated by reference in section 3(a)(74) of the Exchange Act, 15 U.S.C. 78c(a)(74). Pursuant to the definition, the Board of Governors of the Federal Reserve System ("Federal Reserve Board"), the Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, the Farm Credit Administration, or the Federal Housing Finance Agency (collectively, the "prudential regulators") is the "prudential regulator" of a security-based swap dealer or major security-based swap participant if the entity is directly supervised by that regulator.

[12] Section 712(a)(2) of the Dodd-Frank Act provides in part that the Commission shall "consult and coordinate to the extent possible with the Commodity Futures Trading Commission and the prudential regulators for the purposes of assuring regulatory consistency and comparability, to the extent possible."

In addition, section 752(a) of the Dodd-Frank Act provides in part that "[i]n order to promote effective and consistent global regulation of swaps and security-based swaps, the Commodity Futures Trading Commission, the Securities and Exchange Commission, and the prudential regulators . . . as appropriate, shall consult and coordinate with foreign regulatory authorities on the establishment of consistent international standards with respect to the regulation (including fees) of swaps."

foreign regulatory authorities addressing the regulation of OTC derivatives.[13] Through these discussions and the Commission staff's participation in various international task forces and working groups,[14] we have gathered information about foreign regulatory reform efforts and their impact on and relationship with the U.S. regulatory regime. We have taken this information into consideration in developing this proposal.

C. The Cross-Border Proposing Release

Our prior proposals and final rules regarding the application of Title VII to security-based swap activity carried out in the cross-border context (including to persons engaged in such activities) reflect the global nature of the security-based swap market and its development prior to the enactment of the Dodd-Frank Act.[15] We also noted our preliminary belief that dealing activity carried out by a non-U.S. person through a branch, office, affiliate, or an agent acting on its behalf in the United States may raise concerns that Title VII addresses, even if a significant proportion—or all—of those transactions involve non-U.S.-person counterparties.[16] We initially proposed to require any non-U.S. person engaged in dealing activity to include in its de minimis calculation any "transaction conducted within the United States." Thus, under the Cross-Border

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13 Senior representatives of authorities with responsibility for regulation of OTC derivatives have met on a number of occasions to discuss international coordination of OTC derivatives regulations. See, e.g., Report of the OTC Derivatives Regulators Group ("ODRG") on Cross-Border Implementation Issues November 2014 (November 7, 2014), available at: http://www.cftc.gov/ucm/groups/public/@internationalaffairs/documents/file/oia_odrgreportg20_1114.pdf.

14 Commission representatives participate in the Financial Stability Board's Working Group on OTC Derivatives Regulation ("ODWG"), both on the Commission's behalf and as the representative of the International Organization of Securities Commissions ("IOSCO"), which is co-chair of the ODWG. A Commission representative also serves as one of the co-chairs of the IOSCO Task Force on OTC Derivatives Regulation.

15 See Cross-Border Proposing Release, 78 FR 30975-76; Regulation SBSR Adopting Release, 80 FR 14724.

16 See Cross-Border Proposing Release, 78 FR 31000-01.

Proposing Release, a non-U.S. person engaged in dealing activity would have been required to include in its de minimis calculation any transaction where either the person itself or its counterparty performed relevant security-based swap activity within the United States.

The Cross-Border Proposing Release also included proposed rules regarding the application of the clearing, trade execution, regulatory reporting, and public dissemination requirements. Under the rules proposed in that release, the clearing requirement and the trade execution requirement also would have applied to a "transaction conducted within the United States," a transaction having a U.S.-person counterparty, or a transaction having a counterparty that is a non-U.S. person whose counterparty has a right of recourse against a U.S. person,[17] with certain exceptions.[18] The regulatory reporting requirement under that proposal would have applied to a "transaction conducted within the United States," a transaction in which either side of the security-based swap includes an indirect or direct U.S. person counterparty, a transaction in which a security-based swap dealer or major security-based swap participant is a direct or indirect counterparty to the security-based swap, or a transaction that is cleared through a clearing agency having its principal place of business in the United States.[19] The public dissemination requirement would have applied to a "transaction conducted within the United States," a transaction in which a U.S. person is a direct or indirect counterparty on each side of the security-based swap, a transaction in which at least one direct counterparty is a U.S. person (except in the case of a transaction conducted through a foreign branch), a transaction in which

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[17] In this release, we use the terms "non-U.S. persons whose counterparties have a right of recourse against a U.S. person under a security-based swap," "non-U.S. persons whose obligations under a security-based swap are guaranteed by a U.S. person," and "guaranteed non-U.S. persons" interchangeably.

[18] See initially proposed Exchange Act rules 3Ca-3 and 3Ch-1.

[19] See rule 908(a)(1), as re-proposed in the Cross-Border Proposing Release.

one side includes a U.S. person and the other side includes a non-U.S. person that is a security-based swap dealer, or a transaction cleared through a clearing agency having its principal place of business in the United States.[20]

D. The CFTC Staff Advisory

In November 2013, the CFTC's Division of Swap Dealer and Intermediary Oversight issued a Staff Advisory ("CFTC Staff Advisory") addressing the applicability of the CFTC's transaction-level requirements to certain activity by non-U.S. registered swap dealers arranged, negotiated, or executed by personnel or agents of the non-U.S. swap dealer located in the United States.[21] The CFTC Staff Advisory stated CFTC staff's belief that the CFTC "has a strong supervisory interest in swap dealing activities that occur within the United States, regardless of the status of the counterparties" and that a non-U.S. swap dealer "regularly using personnel or agents located in the U.S. to arrange, negotiate, or execute a swap with a non-U.S. person generally would be required to comply with" the CFTC's transaction-level requirements.[22] On January 8, 2014, the CFTC published a request for comment on various aspects of the CFTC Staff Advisory, including whether the CFTC "should adopt the Staff Advisory as Commission

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[20] See rule 908(a)(2), as re-proposed in the Cross-Border Proposing Release.

[21] See CFTC Staff Advisory No. 13-69, "Division of Swap Dealer and Intermediary Oversight Advisory: Applicability of Transaction-Level Requirements to Activity in the United States" (November 14, 2013), available at: http://www.cftc.gov/ucm/groups/public/@lrlettergeneral/documents/letter/13-69.pdf.

In the Interpretive Guidance and Policy Statement Regarding Compliance with Certain Swap Regulations (July 17, 2013), 78 FR 45292 (July 26, 2013) ("CFTC Cross-Border Guidance"), the CFTC defined transaction-level requirements to include the following: (i) required clearing and swap processing; (ii) margining (and segregation) for uncleared swaps; (iii) mandatory trade execution; (iv) swap trading relationship documentation; (v) portfolio reconciliation and compression; (vi) real-time public reporting; (vii) trade confirmation; (viii) daily trading records; and (ix) external business conduct standards. See CFTC Cross-Border Guidance, 78 FR 45333.

[22] Id. at 2.

policy, in whole or in part."[23] In response to this request, the CFTC received approximately 20 comment letters addressing various aspects of the CFTC Staff Advisory.[24] CFTC staff subsequently extended no-action relief related to the CFTC Staff Advisory until the earlier of September 30, 2015, or the effective date of any CFTC action in response to the CFTC Request for Comment.[25] We understand that the CFTC Staff Advisory and comments received in response to the CFTC Request for Comment are under review at the CFTC.

E. Comments on the Proposed Definition of "Transaction Conducted within the United States" and Application of the Definition in the Cross-Border Proposing Release

A number of commenters on our Cross-Border Proposing Release addressed the definition of "transaction conducted within the United States." Although two commenters supported our proposed use of this defined term,[26] commenters generally criticized the proposed definition. These criticisms generally focused on four areas: the scope of activity potentially captured by the initially proposed defined term, the operational difficulties of implementing the defined term, the costs of implementation, and competitive concerns. Market participants also expressed a variety of views on the application of the regulatory reporting, public dissemination,

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23 See Request for Comment on Application of Commission Regulations to Swaps Between Non-U.S. Swap Dealers and Non-U.S. Counterparties Involving Personnel or Agents of the Non-U.S. Swap Dealers Located in the United States, 79 FR 1347 (January 8, 2014) ("CFTC Request for Comment").

24 The comment file is available at http://comments.cftc.gov/PublicComments/CommentList.aspx?id=1452.

25 See Extension of No-Action Relief: Transaction-Level Requirements for Non-U.S. Swap Dealers, CFTC Letter No. 14-140 (November 14, 2014), available at: http://www.cftc.gov/ucm/groups/public/@lrlettergeneral/documents/letter/14-140.pdf.

26 See Letter from Citadel Letter to SEC, dated August 21, 2013 ("Citadel Letter") at 1-2; Letter from ABA to SEC, dated October 2, 2013 ("ABA Letter") at 3 (noting that the initially proposed conduct-based approach is consistent with longstanding Commission practice but also noting potential ambiguities). One of these commenters supported the initially proposed definition because it would help ensure that Title VII requirements applied to security-based swaps of offshore funds with a connection to the United States. See Citadel Letter at 1-2.

clearing, and trade execution requirements. Several market participants opposed the application of the requirements to "transaction[s] conducted within the United States" because of concerns about workability or the scope of the statute, while other commenters argued that the application of the requirements should be expanded to apply to any "transaction conducted within the United States."[27] In light of these comments and our understanding of the structure of the security-based swap market, we determined that our proposed treatment of "transactions conducted within the United States" would benefit from further consideration and solicitation of further comment.

II. Economic Considerations and Baseline Analysis

A. Broad Economic Considerations

These proposed amendments and re-proposed rule would determine when a non-U.S. person whose obligations under a security-based swap are not guaranteed by a U.S. person and that is not a conduit affiliate is required to include in its dealer de minimis calculation transactions with another non-U.S. person and when certain regulatory requirements apply to these and certain other transactions. To provide context for understanding our proposed rules and the related economic analysis that follows, this section discusses how this particular proposal fits within the Title VII framework and identifies broad economic considerations that we preliminarily believe underlie the proposal's likely economic effects.

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[27] These comments are discussed in further detail below, in Sections III.B.2, IV.D, and V.C. As reflected in our discussion throughout this release, we have carefully considered both the CFTC Staff Advisory and the comments submitted in response to the CFTC's request for comment on the CFTC Staff Advisory in developing this proposal. Moreover, in connection with our statutory obligation to consult with the CFTC in connection with Title VII rulemaking, our staff have engaged in extensive discussion with CFTC staff regarding our proposed rules. We note, however, that our discussion of both the CFTC Staff Advisory and the comments received by the CFTC about it reflects our understanding of these documents. Accordingly, neither our discussions of these documents nor any preliminary views expressed herein should be interpreted as necessarily reflecting the views of any other agency or regulator, including the CFTC.

This analysis considers the effects of the proposed rules on security-based swap market participants and transactions that, as a result of these proposed rules, would be subject to rules that we have already adopted, or that we have proposed but not yet adopted, pursuant to Title VII. In particular, we consider the potential adverse effect on market participants of a security-based swap market that may remain opaque to regulators and market participants and that may lack robust customer protections.[28] We also consider possible competitive disparities arising under current and proposed rules.

Title VII provides a statutory framework for the OTC derivatives market and divides authority to regulate that market between the CFTC (which regulates swaps) and the Commission (which regulates security-based swaps). The Title VII framework requires certain market participants to register with the Commission as security-based swap dealers or major security-based swap participants and subjects such entities to certain requirements. The Title VII framework mandates that we establish rules that apply to certain security-based swap transactions, including mandatory clearing, mandatory trade execution, regulatory reporting, and public dissemination.

These proposed amendments and re-proposed rule, together with our previously adopted rules defining "security-based swap dealer" and "major security-based swap participant" and applying those definitions in the cross-border context, would define the scope of entities and transactions that are subject to the requirements of Title VII. Although these proposed amendments and re-proposed rule do not define the specific substantive requirements, the scope of application that they define will play a central role in determining the overall costs and

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[28] See Section VI.B.2, infra, for further discussion of the economic effects of our proposed application of external business conduct requirements. See Section III.B.4, infra, for a discussion of how our proposed approach would support regulatory transparency.

benefits of particular regulatory requirements, and of the Title VII regulatory framework as a whole.[29] For example, to the extent that the proposed application of the de minimis exception leads to a higher number of registered security-based swap dealers, it is reasonable to expect that the aggregate costs and benefits associated with requirements applicable to such dealers will increase.[30]

Several broad economic considerations have informed our proposed approach to identify transactions between two non-U.S. persons that should be subject to certain Title VII requirements. First, to the extent that a financial group carries out security-based swap business in the United States, our ability to monitor dealers for market manipulation or other abusive practices may be limited, even with respect to a registered security-based swap dealer's security-based swaps with U.S. persons. For example, permitting a financial group to carry out a dealing business with U.S. persons through a registered security-based swap dealer and to hedge transactions arising out of that business in the inter-dealer market using the same personnel operating out of the same branch or office in the United States, but acting on behalf of an unregistered non-U.S.-person affiliate, would limit our ability to obtain records that would facilitate our ability to identify potentially abusive conduct in connection with the U.S. person's transactions with U.S.-person counterparties both within the security-based swap market as well as in markets for related underlying assets, such as corporate bonds. Moreover, a non-U.S. person engaged in dealing activity with non-U.S. persons in the United States but not subject to Regulation SBSR would not be required to report its trades, which could make it more difficult

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[29] See Cross-Border Adopting Release, 79 FR 47327 (stating that the registration and regulation of entities as security-based swap dealers and major security-based swap participants will lead to programmatic costs and benefits).

[30] See Section VI.B.1, infra.

for the Commission to monitor that activity for compliance with the federal securities laws and could reduce the transparency of prices in the security-based swap market in the United States. The proposed rules thus reflect our assessment of the impact that the scope of security-based swap transactions and security-based swap dealers subject to regulatory reporting and relevant security-based swap dealer requirements (such as external business conduct standards and recordkeeping and reporting requirements) may have on our ability to detect abusive and manipulative practices in the security-based swap market.

Second, in formulating these proposed rules, we have taken into account the potential impact that rules adopted as part of the Intermediary Definitions Adopting Release and the Cross-Border Adopting Release might have on competition between U.S. persons and non-U.S. persons when they engage in security-based swap transactions with non-U.S. persons, and the implications of these competitive frictions for market integrity. As noted in prior Commission releases, although the Dodd-Frank Act, including Title VII, seeks to achieve a number of benefits,[31] it also imposes costs on registered security-based swap dealers that unregistered persons are not required to bear.[32] For example, section 15F of the Exchange Act imposes various requirements on registered security-based swap dealers, including capital and margin requirements, recordkeeping and reporting requirements, and external business conduct requirements. While the Commission currently applies similar requirements to registered broker-dealers, Title VII applies these requirements only to persons that are registered as

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[31] See Cross-Border Adopting Release, 79 FR 47280 n.11 (citing Dodd-Frank Act preamble, which states that the Dodd-Frank Act was enacted "[t]o promote the financial stability of the United States by improving accountability and transparency in the financial system, to end 'too big to fail', to protect the American taxpayer by ending bailouts, to protect consumers from abusive financial services practices, and for other purposes").

[32] See id. at 47327.

security-based swap dealers. Under current Exchange Act rule 3a71-3(b)(1)(iii), adopted in the Cross-Border Adopting Release, a non-U.S. person that engages in more than a de minimis amount of dealing activity with non-U.S.-person counterparties using personnel located in the United States may face lower regulatory costs than a U.S. competitor engaging in identical activity, because the non-U.S. person is not required to include such transactions in its de minimis calculation. Competitive disparities may also arise as a result of differences in application of other Title VII requirements between U.S. persons and non-U.S. persons that are engaged in dealing activity using personnel located in the United States. As a result, such a non-U.S. person may be able to offer liquidity to its counterparties on more favorable terms than its U.S. competitors.

Under Exchange Act rule 3a71-3, non-U.S. persons may be able to subsidize their transactions with U.S. persons with profits from transactions with non-U.S. persons, allowing them to gain a competitive advantage with respect to transactions with U.S. persons from other dealing activity that is not subject to Title VII, even though it is carried out using personnel located in a U.S. branch or office. In the absence of the rules being proposed in this release, these competitive effects of disparate regulatory treatment may create an incentive for U.S. persons to use non-U.S.-person affiliates or non-U.S.-person agents that are located in the United States to engage in dealing activity with non-U.S.-person counterparties, because these non-U.S. persons could continue to deal with non-U.S.-person counterparties without being required to comply with any Title VII requirements.[33] This disparity could make transactions with U.S.-

[33] We note that, under Exchange Act rule 3a71-3, a non-U.S.-person affiliate of a U.S. person is not required to include such transactions in its dealer de minimis threshold calculations if that non-U.S. person's counterparties do not have recourse to a U.S. person under the terms of the security-based swap and the non-U.S. person is not a conduit affiliate. See Exchange Act rule

person dealers less attractive than transactions with non-U.S.-person dealers, even if the latter are arranging, negotiating, or executing the transaction using personnel located in a U.S. branch or office.

Moreover, differences in the application of the Title VII regulatory requirements may impose differing direct costs on different counterparties. For example, a non-U.S. person seeking to trade in a security-based swap on a U.S. reference entity may prefer to enter into the transaction with a non-U.S.-person dealer rather than a U.S.-person dealer. Even though both dealers are likely to arrange, negotiate, or execute a transaction on a U.S. reference entity using personnel located in a U.S. branch or office, the non-U.S.-person dealer may be more attractive because, for example, a transaction with that dealer may not involve a requirement to post collateral consistent with Title VII margin requirements or to comply with Regulation SBSR. The prospect of directly incurring the costs associated with compliance with Title VII requirements may cause these non-U.S. persons to prefer dealing with unregistered non-U.S.-person dealers, particularly if they can obtain the benefits associated with arranging, negotiating, or executing such a transaction using personnel located in a U.S. branch or office. The rules being proposed in this release are designed to mitigate this outcome.

Regulatory frictions arising from a difference in the treatment of dealing activity occurring in the United States could fragment security-based swap liquidity into two pools, one for U.S. persons and non-U.S. persons whose obligations under a security-based swap are guaranteed by a U.S. person, and the other for non-U.S. persons. Non-U.S. persons that arrange, negotiate, or execute transactions in connection with their dealing activity using personnel

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3171-3(b)(1)(ii) and (iii) (applying the de minimis exception to cross-border dealing activity of conduit affiliates and non-U.S. persons).

located in a U.S. branch or office may, under current Exchange Act rule 3a71-3(b), seek to limit dealing activity with U.S. persons (for example, by quoting larger spreads to compensate for the expected costs of entity-level requirements) or may entirely refuse to supply liquidity to U.S. persons. This disparity in treatment may provide further incentives for U.S. persons to restructure their business to permit them to carry out their business with non-U.S. persons on similar terms.[34] This incentive may be particularly strong among U.S. dealers that are active in the inter-dealer market.

To the extent that the large inter-dealer market[35] shifts in significant part to non-U.S. dealers as a result of current rules, security-based swap activity in the United States could consist of one very large pool of transactions unregulated under Title VII (inter-dealer trades, and transactions between dealers and non-U.S. person non-dealers) and one much smaller pool limited to transactions between dealers and U.S.-person counterparties. This fragmentation could adversely affect the efficiency of risk sharing among security-based swap market participants, as discussed further in Sections VI.B.4(a) and VI.B.4(b), below.

Different treatment of transactions depending on whether they are arranged, negotiated, or executed by personnel located in a U.S. branch or office may create similar fragmentation among agents that may seek to provide services to foreign dealers. To the extent that using agents with personnel located in the United States results in substantial regulatory costs to foreign dealers, such foreign dealers may prefer and primarily use agents located outside the

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[34] See Section VI.B, infra, for further discussion of potential effects of the proposed rules on non-U.S. persons' incentives to use personnel located in U.S. branches or offices to arrange, negotiate, or execute security-based swap transactions.

[35] See Section II.B.2, infra, for an analysis of the proportion of the security-based swap market that constitutes inter-dealer transactions. For the purposes of this analysis we classify any security-based swap transaction between two ISDA-recognized dealers as inter-dealer activity.

United States, while U.S. dealers may continue to use agents located in the United States. This fragmentation of dealer and agent relationships, as in the case of liquidity fragmentation discussed earlier, may adversely affect the efficiency of risk sharing by security-based swap market participants.

B. Baseline

To assess the economic impact of the proposed amendments and rule described in this release, we are using as our baseline the security-based swap market as it exists at the time of this release, including applicable rules we have already adopted but excluding rules that we have proposed but have not yet finalized.[36] The analysis includes the statutory provisions that currently govern the security-based swap market pursuant to the Dodd-Frank Act as well as rules adopted in the Intermediary Definitions Adopting Release, the Cross-Border Adopting Release, Regulation SBSR, and the Security-Based Swap Data Repository ("SDR") Rules and Core Principles.[37] Our understanding of the market is informed by available data on security-based swap transactions, though we acknowledge the data limit the extent to which we can quantitatively characterize the market. Because these data do not cover the entire market, we have developed an understanding of market activity using a sample that includes only certain portions of the market.

1. Current security-based swap market

Our analysis of the state of the current security-based swap market is based on data obtained from the DTCC Derivatives Repository Limited Trade Information Warehouse

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[36] We also take into account, where appropriate, current industry practice in response to the actions of other regulators, such as the CFTC and the European Securities and Markets Authority.

[37] Exchange Act Release No. 74246 (February 11, 2015), 80 FR 14437 (March 19, 2015). As noted above, we have not yet adopted other substantive requirements of Title VII that may affect how firms structure their security-based swap business and market practices more generally.

("TIW"), especially data regarding the activity of market participants in the single-name credit default swap ("CDS") market during the period from 2008 to 2014. According to data published by the Bank for International Settlements ("BIS"), the global notional amount outstanding in equity forwards and swaps as of June 2014 was $2.43 trillion. The notional amount outstanding in single-name CDS was approximately $10.85 trillion, in multi-name index CDS was approximately $7.94 trillion, and in multi-name, non-index CDS was approximately $678 billion.[38] Our analysis in this release focuses on the data relating to single-name CDS. As we have previously noted, although the definition of "security-based swap" is not limited to single-name CDS, we believe that the single-name CDS transactions that we observe are sufficiently representative of the market and therefore can directly inform the analysis of the security-based swap market.[39]

We preliminarily believe that the data underlying our analysis here provide reasonably comprehensive information regarding single-name CDS transactions and the composition of the single-name CDS market participants. We note that the data available to us from TIW do not

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[38] See Semi-annual OTC derivatives statistics at end-June 2014 (December 2014), Table 19, available at: http://www.bis.org/statistics/dt1920a.pdf.

[39] While other repositories may collect data on transactions in total return swaps on equity and debt, we do not currently have access to such data for these products (or other products that are security-based swaps). In the Cross-Border Proposing Release, we explained that we believed that data related to single-name CDS was reasonable for purposes of this analysis, as such transactions appear to constitute roughly 82% of the security-based swap market as measured on a notional basis. See Cross-Border Proposing Release, 78 FR 31120 n.1301. No commenters disputed these assumptions, and we therefore continue to believe that, although the BIS data reflect the global OTC derivatives market, and not just the U.S. market, these ratios are an adequate representation of the U.S. market.

Also consistent with our approach in that release, with the exception of the analysis regarding the degree of overlap between participation in the single-name CDS market and the index CDS market (cross-market activity), our analysis below does not include data regarding index CDS as we do not currently have sufficient information to identify the relative volumes of index CDS that are swaps or security-based swaps.

encompass those CDS transactions that both: (i) do not involve U.S. counterparties;[40] and (ii) are based on non-U.S. reference entities. Notwithstanding this limitation, we preliminarily believe that the TIW data provide sufficient information to identify the types of market participants active in the security-based swap market and the general pattern of dealing within that market.[41]

(a) Dealing Structures and Participant Domiciles

Dealers occupy a central role in the security based swap market and security-based swap dealers use a variety of business models and legal structures to engage in dealing activity with counterparties in jurisdictions all around the world.[42] As we noted in the Cross-Border Adopting Release and as discussed below in Section III.B.4(a), both U.S.-based and foreign-based entities use certain dealing structures for a variety of legal, tax, strategic, and business reasons.[43] Dealers

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40 We note that TIW's entity domicile determinations may not reflect our definition of "U.S. person" in all cases.

41 The challenges we face in estimating measures of current market activity stem, in part, from the absence of comprehensive reporting requirements for security-based swap market participants. We have adopted rules regarding trade reporting, data elements, and public reporting for security-based swaps that will, when fully implemented, provide us with appropriate measures of market activity. See Regulation SBSR Adopting Release, 80 FR 14699-700.

42 Commission staff analysis of TIW transaction records indicates that approximately 99% of single-name CDS price-forming transactions in 2014 involved an ISDA-recognized dealer. "Price-forming transactions" include all new transactions, assignments, modifications to increase the notional amounts of previously executed transactions, and terminations of previously executed transactions. Transactions terminated, transactions entered into in connection with a compression exercise, and expiration of contracts at maturity are not considered price forming and are therefore excluded, as are replacement trades and all bookkeeping-related trades. See Cross-Border Proposing Release, 78 FR 31121 n.1312. For the purpose of this analysis, the ISDA-recognized dealers are those identified by ISDA as belonging to the dealer group, including JP Morgan Chase, Morgan Stanley, Bank of America, Goldman Sachs, Deutsche Bank, Barclays, Citigroup, UBS, Credit Suisse, RBS Group, BNP Paribas, HSBC, Société Générale, Credit Agricole, Wells Fargo, and Nomura. See, e.g., http://www2.isda.org/functional-areas/research/surveys/operations-benchmarking-surveys/.

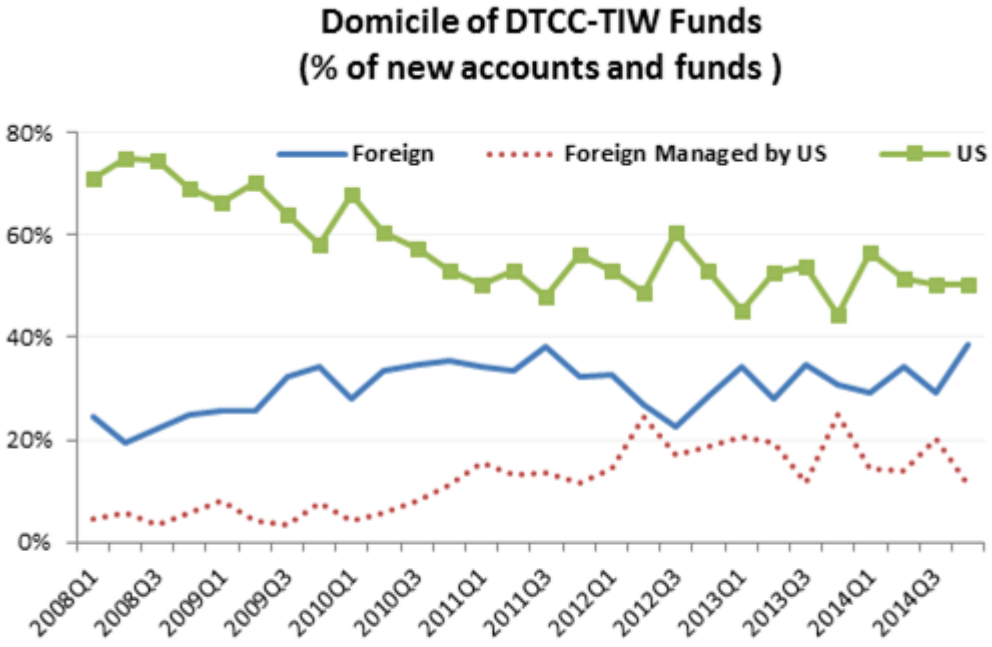
43 See Cross-Border Adopting Release, 79 FR 30976.

may use a variety of structures in part to reduce risk and enhance credit protection based on the particular characteristics of each entity's business.

Bank and non-bank holding companies may use subsidiaries to deal with counterparties. A U.S.-based holding company may engage in dealing activity through a foreign subsidiary that faces both U.S. and foreign counterparties, and foreign dealers may choose to deal with U.S. and foreign counterparties through U.S. subsidiaries. Similarly, a non-dealer user of security-based swaps may participate in the market using an agent in its home country or abroad. An investment adviser located in one jurisdiction may transact in security-based swaps on behalf of beneficial owners that reside in another.

In some situations, an entity's performance under security-based swaps may be supported by a guarantee provided by an affiliate. Such a guarantee may take the form of a blanket guarantee of an affiliate's performance on all security-based swap contracts, or a guarantee may apply only to a specified transaction or counterparty. Guarantees may give counterparties to a dealer direct recourse to the holding company or another affiliate for its dealer-affiliate's obligations under security-based swaps for which that dealer-affiliate acts as counterparty.

Figure 1: The percentage of (1) new accounts with a domicile in the United States (referred to as "US"), (2) new accounts with a domicile outside the United States (referred to below as "Foreign"), and (3) new accounts outside the United States but managed by a U.S. person, account of a foreign branch of a U.S. person, and accounts of a foreign subsidiary of a U.S. person (collectively referred to below as "Foreign Managed by US").[44] Unique, new accounts are aggregated each quarter and percentages are computed on a quarterly basis, from January 2008 through December 2014.



As depicted in Figure 1, the domicile of new accounts participating in the market has shifted over time. A greater share of accounts entering the market either have a foreign domicile, or have a foreign domicile while being managed by a U.S. person. The increase in foreign accounts may reflect an increase in participation by foreign accountholders while the increase in

[44] Following publication of the Warehouse Trust Guidance on CDS data access, TIW surveyed market participants, asking for the physical address associated with each of their accounts (i.e., where the account is organized as a legal entity). This is designated the registered office location by TIW. When an account does not report a registered office location, we have assumed that the settlement country reported by the investment adviser or parent entity to the fund or account is the place of domicile. This treatment assumes that the registered office location reflects the place of domicile for the fund or account.

foreign accounts managed by U.S. persons may reflect the flexibility with which market participants can restructure their market participation in response to regulatory intervention, competitive pressures, and other stimuli. Alternatively, the shifts in new account domicile that we observe in Figure 1 may be unrelated to restructuring or increased foreign participation. For example, changes in the domicile of new accounts over time may reflect improvements in reporting by market participants to TIW rather than a change in market participant structure.[45] Additionally, because the data include only accounts that are domiciled in the United States, that transact with U.S.-domiciled counterparties, or that transact in single-name CDS with U.S. reference entities, changes in the domicile of new accounts may reflect increased transaction activity between U.S. and non-U.S.-person counterparties or increased transactions in single-name CDS on U.S. reference entities by foreign persons.

(b) Market Centers

Participants in the security-based swap market may bear the financial risk of a security-based swap transaction in a location different from the location where the transaction is arranged, negotiated, or executed or the location where economic decisions are made by managers on behalf of beneficial owners. Similarly, a participant in the security-based swap market may be exposed to counterparty risk from a jurisdiction that is different from the market center or centers in which it primarily operates. These participants appear to be active in market centers across the globe.

The TIW transaction records include, in many cases, information on particular branches involved in transactions, which may provide limited insight as to where security-based swap

[45] See note 44, supra.

activity is actually being carried out.[46] These data indicate branch locations located in New York, London, Tokyo, Hong Kong, Chicago, Sydney, Toronto, Frankfurt, Singapore, and the Cayman Islands. Because transaction records in the TIW data provided to us do not indicate explicitly the location in which particular transactions were arranged, negotiated, or executed, these locations may not represent the full set of locations in which activities relevant for these proposed rules take place. Moreover, because we cannot identify the location of transactions within TIW, we are unable to estimate the general distribution of transaction volume across market centers.

(c) Current Estimates of Number of Dealers

In the Regulation SBSR Adopting Release, we estimated, based on an analysis of TIW data, that out of more than 4,000 entities engaged in single-name CDS activity worldwide in 2013, 170 entities engaged in single-name CDS activity at a sufficiently high level that they would be expected to incur assessment costs to determine whether they meet the "security-based swap dealer" definition.[47] Approximately 45 of these entities are non-U.S. persons and are expected to incur assessment costs as a result of engaging in dealing activity with counterparties that are U.S. persons or engaging in dealing activity that involves recourse to U.S. persons.[48] Analysis of those data further indicated that potentially 50 entities may engage in dealing activity

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46 The value of this information is limited in part because some market participants may use business models that do not involve branches to carry out business in jurisdictions other than their home jurisdiction. For example, some market participants may use affiliated or unaffiliated agents to enter into security-based swap transactions in other jurisdictions on their behalf. The available data currently does not allow us to identify with certainty which type of structure is being used in any particular transaction.

47 See Regulation SBSR Adopting Release, 80 FR 14693.

48 See Exchange Act rule 3a71-3(b).

that would exceed the de minimis threshold and thus ultimately have to register as security-based swap dealers.[49]

Updated analysis of 2014 data leaves many of these estimates largely unchanged. We estimate that approximately 170 entities engaged in single-name CDS activity at a sufficiently high level that they would be expected to incur assessment costs to determine whether they meet the "security-based swap dealer" definition. Approximately 56 of these entities are non-U.S. persons. Of the approximately 50 entities that we estimate may potentially register as security-based swap dealers, we preliminarily believe it is reasonable to expect 22 to be non-U.S. persons.

2. Levels of security-based swap trading activity

Single-name CDS contracts make up the vast majority of security-based swaps, and most are written on corporate issuers, corporate securities, sovereign countries, or sovereign debt (reference entities or securities). Figure 2 below describes the percentage of global, notional transaction volume in North American corporate single-name CDS reported to the TIW between January 2008 and December 2013, separated by whether transactions are between two ISDA-recognized dealers (inter-dealer transactions) or whether a transaction has at least one non-dealer counterparty.

Annual trading activity with respect to North American corporate single-name CDS in terms of notional volume has declined from more than $6 trillion in 2008 to less than $3 trillion in 2014.[50] While notional volume has declined over the past six years, the portion of the notional

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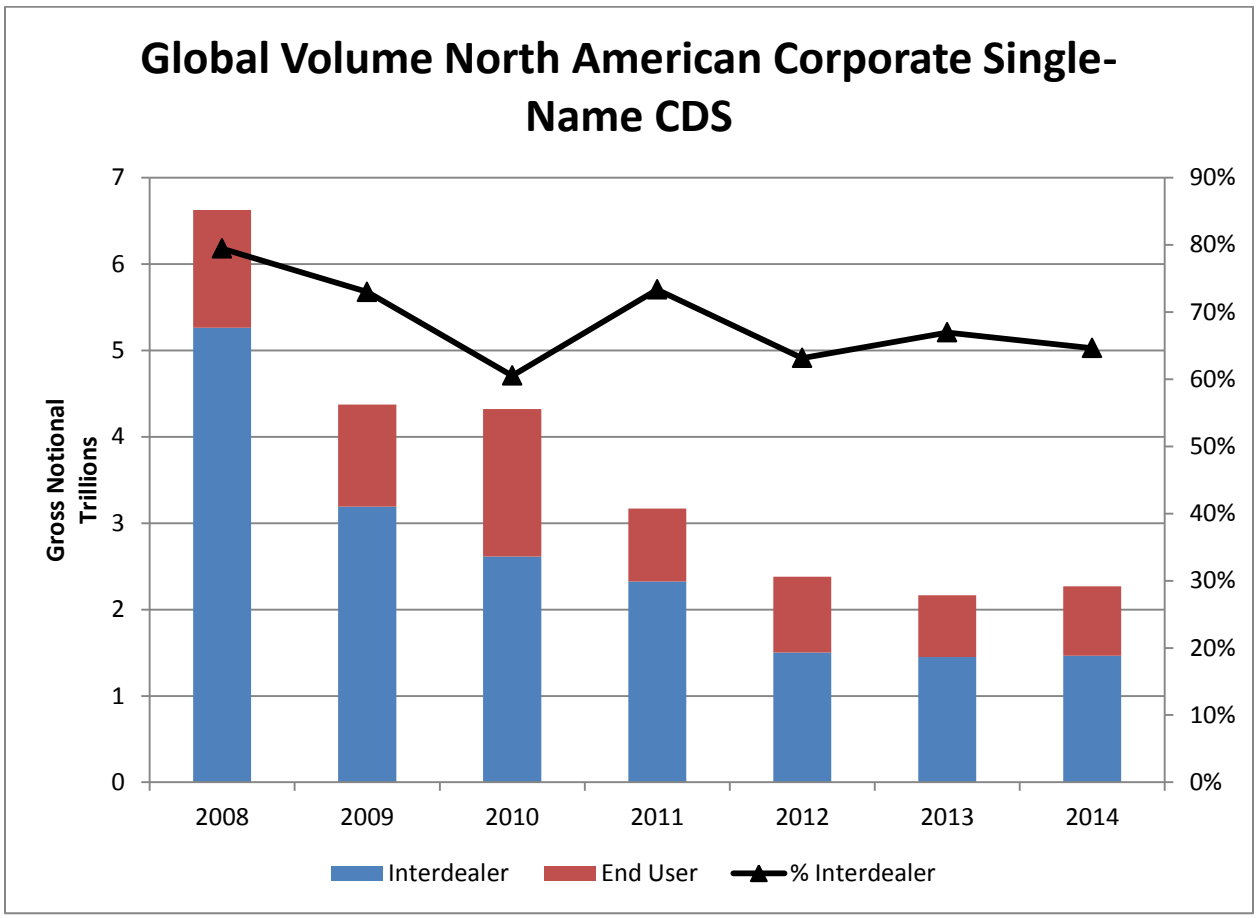
[49] See Regulation SBSR Adopting Release, 80 FR 14693.

[50] The start of this decline predates the enactment of the Dodd-Frank Act and the proposal of rules thereunder, which is important to note for the purpose of understanding the economic baseline for this rulemaking. The timing of this decline seems to indicate that CDS market demand shrank prior to the enactment of the Dodd-Frank Act, and therefore the causes of this reduction in trading volume may be related to market dynamics and not directly related to the enactment of legislation and the development of security-based swap market regulation.

volume represented by inter-dealer transactions has remained fairly constant and inter-dealer transactions continue to represent a significant majority of trading activity, whether measured in terms of notional value or number of transactions (see Figure 2).

The high level of inter-dealer trading activity reflects the central position of a small number of dealers, each of which intermediates trades between many hundreds of counterparties. While we are unable to quantify the current level of trading costs for single-name CDS, those dealers appear to enjoy market power as a result of their small number and the large proportion of order flow they privately observe. This market power in turn appears to be a key determinant of trading costs in this market.

Figure 2: Global, notional trading volume in North American corporate single-name CDS by calendar year and the fraction of volume that is inter-dealer.



Against this backdrop of declining North American corporate single-name CDS activity, about half of the trading activity in North American corporate single-name CDS reflected in the set of data that we analyzed was between counterparties domiciled in the United States and counterparties domiciled abroad. Basing counterparty domicile on the self-reported registered office location of the TIW accounts, we estimate that only 12% of the global transaction volume by notional volume between 2008 and 2014 was between two U.S.-domiciled counterparties, compared to 48% entered into between one U.S.-domiciled counterparty and a foreign-domiciled counterparty and 40% entered into between two foreign-domiciled counterparties (see Figure 3).[51]

When the domicile of TIW accounts is instead defined according to the domicile of an account's ultimate parents, headquarters, or home office (e.g., classifying a foreign bank branch or foreign subsidiary of a U.S. entity as domiciled in the United States), the fraction of transactions entered into between two U.S.-domiciled counterparties increases to 32%, and to 51% for transactions entered into between a U.S.-domiciled counterparty and a foreign-domiciled counterparty.

Differences in classifications across different definitions of domicile illustrate the effect of participant structures that operate across jurisdictions. Notably, the proportion of activity between two foreign-domiciled counterparties drops from 40% to 17% when domicile is defined as the ultimate parent's domicile. As noted earlier, foreign subsidiaries of U.S. parent companies and foreign branches of U.S. banks, and U.S. subsidiaries of foreign parent companies and U.S.

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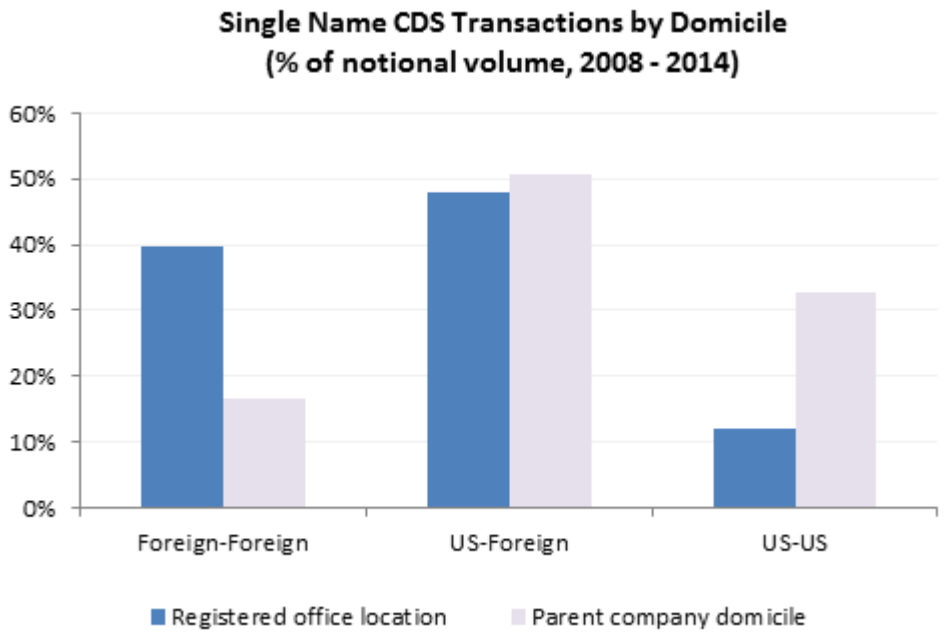
[51] See note 44, supra. For purposes of this discussion, we have assumed that the registered office location reflects the place of domicile for the fund or account, but we note that this domicile does not necessarily correspond to the location of an entity's sales or trading desk.

branches of foreign banks may transact with U.S. and foreign counterparties. However, this change in respective shares based on different classifications suggests that the activity of foreign subsidiaries of U.S. firms and foreign branches of U.S. banks is generally higher than the activity of U.S. subsidiaries of foreign firms and U.S. branches of foreign banks.

Figure 3: The fraction of notional volume in North American corporate single-name CDS between (1) two U.S.-domiciled accounts, (2) one U.S.-domiciled account and one non-U.S.-domiciled account, and (3) two non-U.S.-domiciled accounts, computed from January 2008 through December 2014.



3. Regulatory reporting, clearing, and trade execution of security-based swap transactions

We have adopted final rules implementing regulatory reporting requirements for security-based swap transactions, although compliance with most aspects of this regime is not yet required.[52] Although counterparties are not yet required to comply with rules that require them to report transaction information, virtually all market participants voluntarily report their trades

[52] See Regulation SBSR Adopting Release, 80 FR 14566.

in single-name CDS to TIW, which maintains a record of these transactions, in some cases with the assistance of post-trade processors.[53] Among other things, this centralized record-keeping facilitates settlement of obligations between counterparties when a default event occurs as well as bulk transfers of positions between accounts at a single firm or between firms.

Clearing of security-based swaps, which is currently voluntary in the United States, is currently limited to CDS products, and a substantial proportion of single-name CDS accepted for clearing are already being cleared. Prior to the Dodd-Frank Act, ICE Clear Credit and ICE Clear Europe engaged in CDS clearing activities pursuant to exemptive orders issued by the Commission.[54] Pursuant to the Dodd-Frank Act, ICE Clear Credit and ICE Clear Europe were deemed to be registered with the Commission in July 2011 as clearing agencies for security-based swaps.[55] ICE Clear Credit began clearing corporate single-name CDS in December 2009,[56] and, as of March 17, 2015, had cleared a total of $3.06 trillion gross notional of single-

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53 See http://www.isdacdsmarketplace.com/exposures_and_activity (last visited September 22, 2014).

54 See, e.g., Exchange Act Release No. 59527 (March 6, 2009), 74 FR 10791 (March 12, 2009) ("ICE Clear Credit Exemptive Order"); Exchange Act Release No. 60372 (July 23, 2009), 74 FR 37748 (July 29, 2009) ("ICE Clear Europe Exemptive Order"). In connection with those orders, Commission considered clearing practices of those central counterparties ("CCPs"), including, inter alia, their risk management methodologies.

55 Section 17A(l) of the Exchange Act provides in relevant part that a derivative clearing organization registered with the CFTC that clears security-based swaps would be deemed to be registered as a clearing agency under section 17A if, prior to the enactment of the Dodd-Frank Act, it cleared swaps pursuant to an exemption from registration as a clearing agency. Both ICE Clear Credit and ICE Clear Europe also are registered with the CFTC as derivative clearing organizations.

56 See Exchange Act Release No. 61662 (March 5, 2010), 75 FR 11589, 11591 (March 11, 2010) (discussing ICE Clear Credit's CDS clearing activities as of March 2010).

ICE Clear Credit (then known as ICE US Trust LLC) began clearing index CDS in March 2009. See Exchange Act Release No. 59527 (March. 6, 2009), 74 FR 10791 (March 12, 2009) (order granting temporary exemptions under the Exchange Act on behalf of ICE US Trust LLC).

name CDS on 368 North American and European instruments.[57] As of the beginning of this year, ICE Clear Credit accepted for clearing a total of 207 CDS products based on North American instruments, 168 CDS products based on European instruments, and fifteen CDS products based on individual sovereign (nation-state) reference entities.

Staff analysis of trade activity from July 2012 to December 2013 indicate that, out of $938 billion of notional traded in North American corporate single-name CDS contracts that have reference entities that are accepted for clearing during the 18 months ending December 2013, approximately 71%, or $666 billion, had characteristics making them suitable for clearing by ICE Clear Credit and represented trades between two ICE Clear Credit clearing members. Approximately 79% of this notional value, or $525 billion, was cleared through ICE Clear Credit, or 56% of the $938 billion in new trade activity.

Figure 4 shows the proportion of new trades and assign-entries defined as clearable at ICE Clear Credit that were ultimately cleared.[58]

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57 ICE Clear Credit also has cleared a total of $37.3 trillion gross notional on 137 index CDS as of March 20, 2015. See ICE Clear Credit, Volume of ICE CDS Clearing, available at: https://www.theice.com/clear_credit.jhtml.

In addition to clearing single-name CDS on North American corporate reference entities, ICE Clear Credit also clears CDS on certain non-U.S. sovereign entities, and on certain indices based on North American reference entities.

58 For the purposes of this analysis, "clearable" describes CDS contracts on North American single-name corporate reference entities between clearing members that reference the ISDA Standard North American Corporate (SNAC) documentation, are denominated in U.S. dollars, do not include restructuring as a credit event and have a standard coupon. If ICE Clear Credit accepts CDS on the reference entity for clearing, then a standard coupon is one that is accepted for clearing for that reference entity by ICE Clear Credit; otherwise, standard coupon means a coupon of either 100 or 500 basis points. See SEC Division of Economic and Risk Analysis, Single-Name Corporate Credit Default Swaps: Background Data Analysis on Voluntary Clearing Activity, 15 (April 2015), available at http://www.sec.gov/dera/staff-papers/white-papers/voluntary-clearing-activity.pdf.

Evidence from the TIW data suggests that even single-name CDS written on reference entities that were initially accepted for clearing by ICE Clear Credit were traded infrequently. Figure 5 plots of the daily mean number of transactions per trading day for each of the 538 North American single-name corporate reference entities with at least one transaction per month on average during the period from January 2011 to December 2013.[59] Each vertical bar represents the mean number of transactions per day for a reference entity.[60] The 538 reference entities are presented in decreasing order of the mean number of transactions per trading day. Commission staff has identified the 68 reference entities in the sample that were cleared by ICE Clear Credit prior to the enactment of the Dodd-Frank Act (the "deemed submitted" reference entities). The 68 deemed submitted reference entities are marked by Xs forming a line near the horizontal axis. The remaining Xs (those not on the line of Xs near the horizontal axis) represent, for each reference entity, the fraction of days with no transactions. The evidence in Figure 5 suggests that within the sample period, the most traded entity of the 68 "deemed submitted" reference entities was traded approximately 15 times per day on average. Despite the low average number of transactions per day, these 68 reference entities generally have a lower proportion of days with no transactions relative to the rest of the single-name CDS market represented in the sample.

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59 We analyze single-name corporate reference entities with at least one transaction per month on average from January 2011 to December 2013 to avoid including outliers that trade extremely infrequently. Of the 573 North American single-name corporate reference entities with at least 36 transactions included in Figure 5, only 538 had at least 36 new trades, implying that the other 35 had price forming transactions that were not associated with new trading activity, such as terminations or assignments. See id. at 41.

60 Transaction types include all price forming transactions: new trades, amendments that change economic terms of the contract, assignments, and terminations.

ICE Clear Europe began clearing CDS on single-name corporate reference entities in December 2009,[61] and, as of March 17, 2015, had cleared a total €2.48 trillion in gross notional of single-name CDS on 161 European corporate reference entities.[62] As of the beginning of 2015, ICE Clear Europe accepted for clearing a total of 161 CDS products based on European corporate reference entities.

Staff analysis of new trade activity from July 2012 to December 2013 indicate that out of €531 billion of notional traded in European corporate single-name CDS contracts that have reference entities that are accepted for clearing during the 18 months ending December 2013, approximately 70%, or €372 billion had characteristics making them suitable for clearing by ICE Clear Europe and represented trades between two ICE Clear Europe clearing members. Approximately 51% of this notional value, or €191 billion was cleared through ICE Clear Europe, representing 36% of the total volume of new trade activity.[63]

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61 See Exchange Act Release No. 61973 (April 23, 2010), 75 FR 22656, 22657 (April 29, 2010) (discussing ICE Clear Europe's CDS clearing activity as of April 2010).

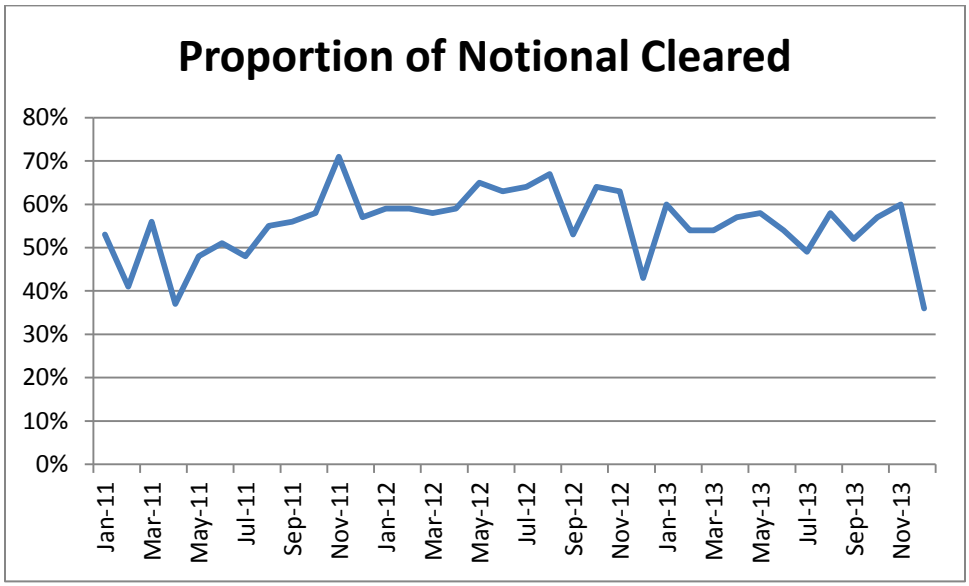
ICE Clear Europe commenced clearing index CDS in July 2009. See Exchange Act Release No. 60372 (July 23, 2009), 74 FR 37748 (July 29, 2009) (order granting temporary exemptions under the Exchange Act on behalf of ICE Clear Europe).

62 ICE Clear Europe also has cleared a total of €14.4 trillion in gross notional on 64 index CDS as of March 20, 2015. See ICE Clear Europe, Volume of ICE CDS Clearing, available at: https://www.theice.com/clear_credit.jhtml.

Aside from clearing single-name CDS on European corporate reference entities, ICE Clear Europe also clears CDS on indices based on European reference entities, as well as futures and instruments on OTC energy and emissions markets.

63 These numbers do not include transactions in European corporate single-name CDS that were cleared by ICE Clear Credit. However, during the sample period, there was only one day on which there were transactions that were cleared by ICE Clear Credit (December 20, 2013) and the traded notional of these transactions was minimal. For historical data, see https://www.theice.com/marketdata/reports/99.

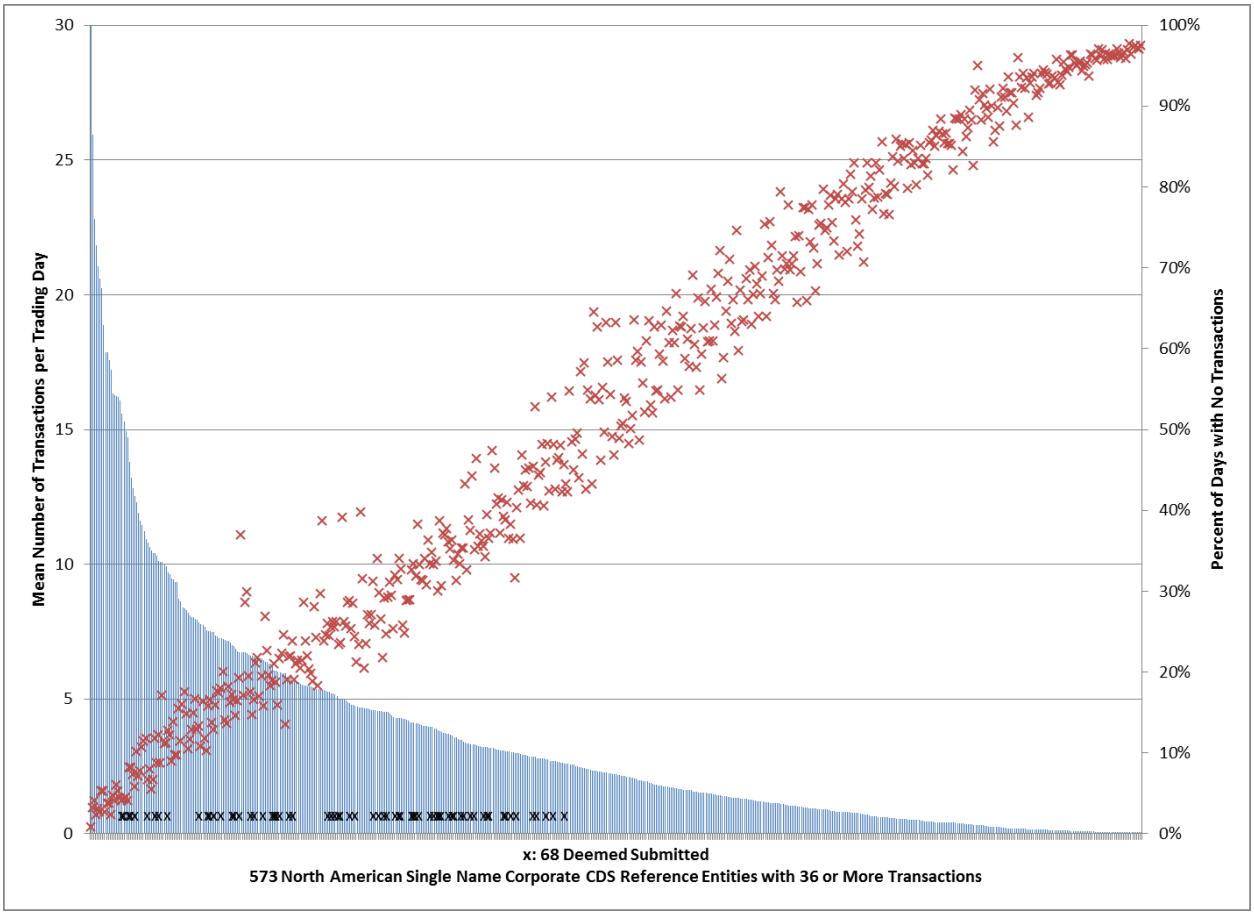
Figure 4: The fraction of total gross notional amount of new trades and assign-entries in North American single-name CDS products that was clearable at ICE Clear Credit, and was cleared within 14 days of the initial transaction.[64]



64 We preliminarily believe that it is reasonable to assume that, when clearing occurs within 14 days of execution, counterparties made the decision to clear at the time of execution and not as a result of information arriving after execution.

An "assign-entry" involves the substitution of one of the contract counterparties in an existing instrument for a new counterparty in exchange for cash consideration. It is economically equivalent to a termination of the initial contract between the "old" counterparty and the "static" counterparty and a new trade between the "replacement" counterparty and the "static" counterparty.

Figure 5. North American Single-Name Corporate CDS Transaction Activity: January 2011–December 2013



Unlike the markets for cash equity securities and listed options, the market for security-based swaps is characterized almost exclusively by bilateral OTC negotiation and is largely decentralized.[65] The lack of uniform rules concerning the trading of security-based swaps and the historical one-to-one nature of trade negotiation in security-based swaps has resulted in the formation of distinct types of trading venues and execution practices, ranging from bilateral negotiations carried out over the telephone,[66] single-dealer RFQ platforms,[67] multi-dealer RFQ

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65 See SB SEF Proposing Release, 76 FR 10951.

66 "Bilateral negotiation" refers to the execution practice whereby one party uses telephone, e-mail, or other communication methods to contact directly a potential counterparty to negotiate and

platforms,[68] central limit order books,[69] and brokerage trading.[70] These various trading venues and execution practices provide different degrees of pre-trade transparency and afford market participants different levels of access. We currently do not have sufficient information with respect to the volume of security-based swap transactions executed across these different trading venues and using these various execution practices.

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execute a security-based swap. The bilateral negotiation and execution practice provides no pre-trade or post-trade transparency because only the two parties to the transaction are aware of the terms of the negotiation and the final terms of the agreement. See SB SEF Proposing Release, 76 FR 10951.

67 A single-dealer RFQ platform refers to an electronic trading platform where a dealer may post indicative quotes for security-based swaps in various asset classes that the dealer is willing to trade. Only the dealer's approved customers would have access to the platform. When a customer wishes to transact in a security-based swap, the customer requests an executable quote, the dealer provides one, and if the customer accepts the dealer's quote, the transaction is executed electronically. This type of platform generally provides pre-trade transparency in the form of indicative quotes on a pricing screen, but only from one dealer to its customer. See SB SEF Proposing Release, 76 FR 10951.

68 A multi-dealer RFQ electronic trading platform refers to a multi-dealer RFQ system whereby a requester can send an RFQ to solicit quotes on a certain security-based swap from multiple dealers at the same time. After the RFQ is submitted, the recipients have a prescribed amount of time in which to respond to the RFQ with a quote. Responses to the RFQ are firm. The requestor then has the opportunity to review the responses and accept the best quote. A multi-dealer RFQ platform provides a certain degree of pre-trade transparency, depending on its characteristics. See SB SEF Proposing Release, 76 FR 10952.

69 A limit order book system or similar system refers to a trading system in which firm bids and offers are posted for all participants to see, with the identity of the parties withheld until a transaction occurs. Bids and offers are then matched based on price-time priority or other established parameters and trades are executed accordingly. The quotes on a limit order book system are firm. In general, a limit order book system provides greater pre-trade transparency than the three models described above because all participants can view bids and offers before placing their bids and offers. See SB SEF Proposing Release, 76 FR 10952. Currently, limit order books for the trading of security-based swaps in the United States are utilized by inter-dealer brokers for dealer-to-dealer transactions.

70 "Brokerage trading" refers to an execution practice used by brokers to execute security-based swaps on behalf of customers, often in larger-sized or bespoke transactions. In such a system, a broker receives a request from a customer (which may be a dealer) that seeks to execute a specific type of security-based swap. The broker then interacts with other customers to fill the request and execute the transaction. This model often is used by dealers that seek to transact with other dealers through the use of an inter-dealer broker as an intermediary. In this model, there may be pre-trade transparency to the extent that participants are able to see bids and offers of other participants. See SB SEF Proposing Release, 76 FR 10952.

We have proposed, but have not yet adopted, rules establishing a registration regime and core principles for security-based swap execution facilities ("SB SEFs"). We have not proposed to implement the mandatory trade execution requirement contained in section 3C(h) of the Exchange Act. Currently, there are no SB SEFs registered with the Commission, and as a result, there is no registered SB SEF trading activity to report. There are, however, currently 25 trading platforms that either are temporarily registered with the CFTC as SEFs or have SEF temporary registration applications pending with the CFTC and currently are exempt from registration with the Commission.[71] As we discuss in Section II.B.5, the cash flows of security-based swaps and swaps are closely related and many participants in the security-based swap also participate in the swap market and so we preliminarily believe that many SEFs that currently serve as trading venues for swaps are likely also to register with the Commission as SB SEFs. However, owing to the smaller size of the security-based swap market, we currently expect that there will be fewer exchanges and SB SEFs that will eventually host transactions in security-based swaps than the 25 SEFs reported within the CFTC's jurisdiction.

4. Global regulatory efforts

Efforts to regulate the swaps market are underway not only in the United States but also abroad, and these efforts have received significant attention in international fora. For example, in 2009, leaders of the G20—whose membership includes the United States, 18 other countries, and the EU—addressed global improvements in the functioning, transparency, and regulatory

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[71] See Effective Date Release, 76 FR at 36306 (exempting persons that operate a facility for the trading or processing of security-based swaps that is not currently registered as a national securities exchange, or that cannot yet register as an SB SEF because final rules for such registration have not yet been adopted, from the requirements of Section 3D(a)(1) of the Exchange Act until the earliest compliance date set forth in any of the final rules regarding registration of SB SEFs). A list of platforms that either are temporarily registered with the CFTC or have SEF temporary registration applications pending with the CFTC is available at: http://sirt.cftc.gov/SIRT/SIRT.aspx?Topic=SwapExecutionFacilities (last visited March 2, 2015).

oversight of OTC derivatives markets. They expressed their view on a variety of issues relating to OTC derivatives contracts, including trading on exchanges or electronic trading platforms, clearing through CCPs, and reporting to trade repositories.[72] In subsequent summits, the G20 leaders have returned to OTC derivatives regulatory reform and encouraged international consultation in developing standards for these markets.[73]

Jurisdictions with major OTC derivatives markets have taken steps toward substantive regulation of these markets, though the pace of regulation varies. Accordingly, many foreign participants likely will be required to comply with substantive regulation of their security-based swap activities apart from regulations that may apply to them pursuant to Title VII. The concerns foreign jurisdictions seek to address with their regulations may overlap or be similar to those addressed by the Title VII regulatory framework.

Foreign legislative and regulatory efforts have focused on five general areas: requiring post-trade reporting of transactions data for regulatory purposes, moving OTC derivatives onto organized trading platforms, requiring central clearing of OTC derivatives, establishing or enhancing capital requirements, and establishing or enhancing margin requirements for OTC derivatives transactions. The first two areas of regulation should help improve transparency in OTC derivatives markets, both to regulators and market participants. Regulatory transaction reporting requirements are mandated in a number of jurisdictions including the EU, Hong Kong SAR, Japan, and Singapore; other jurisdictions are in the process of proposing legislation and

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72 See G20 Leaders' Statement, Pittsburgh, United States, September 24-25, 2009, available at: http://www.treasury.gov/resource-center/international/g7-g20/Documents/pittsburgh_summit_leaders_statement_250909.pdf.

73 See the G20 Leaders Communique (November 2014), para. 12, available at: https://www.g20.org/sites/default/files/g20_resources/library/brisbane_g20_leaders_summit_communique.pdf.

rules to implement these requirements.[74] The EU has adopted legislation for markets in financial instruments that addresses trading OTC derivatives on regulated trading platforms.[75] This legislation also should promote post-trade public transparency in OTC derivatives markets by requiring the price, volume, and time of derivatives transactions conducted on these regulated trading platforms to be made public in as close to real time as technically possible.[76]

Regulation of derivatives central clearing, capital requirements, and margin requirements aims, among other things, to improve management of financial risks in these markets.[77] Japan has rules in force mandating central clearing of certain OTC derivatives transactions.[78] The EU has its legislation in place but has not yet made any determinations of specific OTC derivatives transactions subject to mandatory central clearing. Most other jurisdictions are still in the process of formulating their legal frameworks that govern central clearing. A number of major foreign jurisdictions have initiated the process of drafting rules to implement margin requirements for OTC derivatives transactions.

5. Cross-market participation

Persons registered as security-based swap dealers or major security-based swap participants are likely also to engage in swap activity, which is subject to regulation by the CFTC. In the release proposing registration requirements for security-based swap dealers and

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[74] Information regarding ongoing regulatory developments described in this section was primarily obtained from progress reports published by the Financial Stability Board. These are available at: http://www.financialstabilityboard.org/list/_fsb_publications/index.htm.

[75] See id.

[76] See Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) no 648/2012), available at: http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32014R0600&from=EN.

[77] See note 74, supra.

[78] See id.

major security-based swap participants, we estimated, based on our experience and understanding of the swap and security-based swap markets that of the 55 firms that might register as security-based swap dealers or major security-based swap participants, approximately 35 would also register with the CFTC as swap dealers or major swap participants.[79] Available data suggest that these numbers remain largely unchanged.[80]

This overlap reflects the relationship between single-name CDS contracts, which are security-based swaps, and index CDS contracts, which may be swaps or security-based swaps. A single-name CDS contract covers default events for a single reference entity or reference security. Index CDS contracts and related products make payouts that are contingent on the default of index components and allow participants in these instruments to gain exposure to the credit risk of the basket of reference entities that comprise the index, which is a function of the credit risk of the index components. A default event for a reference entity that is an index component will result in payoffs on both single-name CDS written on the reference entity and index CDS written on indices that contain the reference entity. Because of this relationship between the payoffs of single-name CDS and index CDS contracts, prices of these products depend upon one another,[81] creating hedging opportunities across these markets.

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79 See Registration of Security-Based Swap Dealers and Major Security-Based Swap Participants, Exchange Act Release No. 65543 (October 12, 2011), 76 FR 65784, 65808 (October 24, 2011).

80 Based on its analysis of 2014 TIW data and the list of swap dealers provisionally-registered with the CFTC, and applying the methodology used in the Intermediary Definitions Adopting Release, we estimate that substantially all registered security-based swap dealers would also register as swap dealers with the CFTC. See also CFTC list of provisionally registered swap dealers, available at: http://www.cftc.gov/LawRegulation/DoddFrankAct/registerswapdealer.

81 "Correlation" typically refers to linear relationships between variables; "dependence" captures a broader set of relationships that may be more appropriate for certain swaps and security-based swaps. See, e.g., Casella, George and Roger L. Berger, Statistical Inference (2002), at 171.

These hedging opportunities mean that participants that are active in one market are likely to be active in the other. Commission staff analysis of approximately 4,500 TIW accounts that participated in the market for single-name CDS in 2014 revealed that approximately 2,500 of those accounts, or 56%, also participated in the market for index CDS. Of the accounts that participated in both markets, data regarding transactions in 2014 suggest that, conditional on an account transacting in notional volume of index CDS in the top third of accounts, the probability of the same account landing in the top third of accounts in terms of single-name CDS notional volume is approximately 60%; by contrast, the probability of the same account landing in the bottom third of accounts in terms of single-name CDS notional volume is only 11%.

As discussed in more detail below,[82] the CFTC Staff Advisory issued in November 2013 stated the CFTC staff's belief that the CFTC has a strong supervisory interest in swap dealing activities that occur within the United States, regardless of the status of the counterparties. The CFTC Staff Advisory, which we understand to be under review at the CFTC,[83] also stated the CFTC staff's belief that a non-U.S. swap dealer "regularly using personnel or agents located in the U.S. to arrange, negotiate, or execute a swap with a non-U.S. person generally would be required to comply with" the CFTC's transaction-level requirements.[84] While CFTC staff has granted relief from certain aspects of the CFTC Staff Advisory,[85] at least one commenter has argued that the CFTC's approach to regulation of swap dealers taken in the CFTC Cross-Border Guidance has influenced the information that market participants collect and maintain about the

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82 See Section III.B.3, infra.

83 See CFTC Request for Comment.

84 See CFTC Staff Advisory at 1-2.

85 See note 25, supra.

swap transactions they enter into and the counterparties they face.[86] Although that commenter suggested that swap market participants have also adopted business practices consistent with the CFTC Cross-Border Guidance, the commenter did not supply particular details as to the scope of the changes to its operations.[87]

The proposed amendments and proposed rule may, to the extent that they are not in conflict with the approach taken in the CFTC Cross-Border Guidance, permit non-U.S. persons to use infrastructures developed to be consistent with the CFTC's approach, to comply with Commission requirements as well. Among those entities that participate in both markets, entities that are able to apply to security-based swap activity capabilities that are consistent with the CFTC Cross-Border Guidance may experience lower costs associated with assessing which cross-border security-based swap activity counts against the dealer de minimis exception or towards the major participant threshold, relative to those that are unable to redeploy such capabilities. We remain sensitive to the fact that in cases where our final rules differ from the CFTC approach, additional outlays related to information collection and storage may be required.

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86 See, e.g., Letter from Securities Industry and Financial Markets Association/Futures Industry Association/Financial Services Roundtable ("SIFMA/FIA/FSR") to SEC, dated August 21, 2013 ("SIFMA/FIA/FSR Letter") at 2-3.

87 Id. at 2-4. The commenter notes the "technological, operational, legal and compliance systems" necessary for complying with our proposed rules, and taking account of the CFTC Cross-Border Guidance, outlining the general categories of changes to practice necessary for compliance. Id. The commenter further indicates a potential need to "build[] separate systems for a small percentage of the combined swaps and SBS market instead of using the systems already built for compliance with the CFTC's cross-border approach," suggesting that market participants have adopted market practices consistent with the CFTC Cross-Border Guidance. Id.

III. Application of the Dealer De Minimis Exception to U.S. Security-Based Swap Dealing Operations of Non-U.S. Persons

A. Overview

The Exchange Act excepts from designation as a "security-based swap dealer" an entity that engages in a "de minimis" quantity of security-based swap dealing activity with or on behalf of customers.[88] Under the final rules adopted in the Intermediary Definitions Adopting Release, a person may take advantage of that exception if, in connection with credit default swaps that constitute security-based swaps, the person's dealing activity over the preceding 12 months does not exceed a gross notional amount of $3 billion, subject to a phase-in level of $8 billion.[89] The phase-in level will remain in place until—following a study regarding the definitions of "security-based swap dealer" and "major security-based swap participant"—we either terminate the phase-in period or establish an alternative threshold following rulemaking.[90]

The Cross-Border Adopting Release finalized rules specifying, among other things, when a non-U.S. person is required to include transactions arising from its dealing activity in its de minimis threshold calculations.[91] These final rules addressed the application of the security-based swap dealer de minimis exception to such person's dealing activity involving U.S.-person

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88 See Exchange Act section 3(a)(71)(D).

89 See Exchange Act rule 3a71-2(a)(1)(i). Lower thresholds are set forth in connection with dealing activity involving other types of security-based swaps. See Exchange Act rule 3a71-2(a)(1)(ii).

90 See Intermediary Definitions Adopting Release, 77 FR 30640-41. Exchange Act rule 3a71-2 establishes a phase-in period during which the de minimis threshold will be $8 billion and during which Commission staff will study the security-based swap market as it evolves under the new regulatory framework, resulting in a report that will consider the operation of the "security-based swap dealer" and "major security-based swap participant" definitions. In that release we explained that at the end of the phase-in period, we will take into account the report, as well as public comment on the report, in determining whether to terminate the phase-in period or propose any changes to the rule implementing the de minimis exception, including any increases or decreases to the $3 billion threshold. See id. at 30640.

91 See Cross-Border Adopting Release, 79 FR 47319-322. See also Exchange Act rules 3a71-3(b), 3a71-4.

counterparties, as well as the dealing activity of a non-U.S. person that is a conduit affiliate[92] or whose counterparty has a right of recourse under the security-based swap against an affiliated U.S. person.[93] Although we had proposed requiring a non-U.S. person to include in this calculation any dealing activity involving another non-U.S.-person counterparty if it resulted in a "transaction conducted within the United States" as defined in the proposed rule,[94] we did not address this issue in our Cross-Border Adopting Release. As we noted in that adopting release, commenters raised a number of significant issues related to this element of the Cross-Border Proposing Release, including our authority to impose, and the costs of complying with, this requirement, and we determined that final resolution of this issue would benefit from further consideration and public comment.[95]

In light of those comments and further consideration of the concerns raised by such transactions and subsequent regulatory and market developments, the statutory objectives, and the practicability of our initially proposed approach, we have determined to propose an amendment to Exchange Act rules 3a71-3 and 3a71-5 that more closely focuses on certain dealing activity carried out, at least in part, by personnel located in the United States.[96] The proposed amendments would not require a non-U.S. person engaging in dealing activity to consider the location of its non-U.S.-person counterparty or that counterparty's agent in determining whether the transaction needs to be included in its own de minimis calculation. Instead, the proposed amendments would require a non-U.S. person to include in its de minimis

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92 See Exchange Act rule 3a71-3(a)(1); Cross-Border Adopting Release, 79 FR 47313.

93 See Cross-Border Adopting Release, 79 FR 47316.

94 See Cross-Border Proposing Release, 78 FR 30999-31001.

95 See, e.g., Cross-Border Adopting Release, 79 FR 47280.

96 See proposed Exchange Act rule 3a71-3(b)(1)(iii)(C); proposed Exchange Act rule 3a71-5(c).

calculation any transaction connected with its security-based swap dealing activity that it enters into with a non-U.S.-person counterparty only when the transaction is arranged, negotiated, or executed by personnel of the non-U.S. person located in a U.S. branch or office, or by personnel of such person's agent located in a U.S. branch of office.

As described in more detail below, we preliminarily believe that this proposed approach would mitigate many of the concerns raised by commenters in response to our initial proposal, while requiring persons that engage in dealing activity at levels that may raise the types of concerns that Title VII addresses to register as security-based swap dealers and comply with appropriate regulation. We also note that this approach would be generally consistent with the approach that we have followed with respect to the registration of brokers and dealers under the Exchange Act, which among other things requires that a broker-dealer physically operating in the United States register with the Commission and comply with relevant regulatory requirements, even if it directs its activities solely toward non-U.S. persons outside the United States.[97]

B. Proposed Application of De Minimis Exception to Non-U.S. Persons Arranging, Negotiating, or Executing Security-Based Swap Transactions Using Personnel Located in a U.S. Branch or Office

1. Overview of the initially proposed approach

As we noted in the Cross-Border Proposing Release, dealing activity carried out by a non-U.S. person through a U.S. branch, office, or affiliate or by a non-U.S. person that otherwise engages in security-based swap dealing activity in the United States, particularly at levels exceeding the relevant de minimis thresholds, may raise concerns that Title VII addresses, even if a significant proportion—or all—of those transactions involve non-U.S.-person

[97] See Registration Requirements for Foreign Broker-Dealers, Exchange Act Release No. 27017 (July 11, 1989), 54 FR 30013 (July 18, 1989).

counterparties.[98] Accordingly, we initially proposed to require any non-U.S. person to include in its de minimis calculation any security-based swap transaction connected with its dealing activities that is a "transaction conducted within the United States."[99] We proposed to define "transaction conducted within the United States" as any "security-based swap transaction that is solicited, negotiated, executed, or booked within the United States, by or on behalf of either counterparty to the transaction, regardless of the location, domicile, or residence status of either counterparty to the transaction."[100] Thus, under this initially proposed definition, a non-U.S. person engaged in dealing activity would have been required to include in its de minimis calculation any transaction where either the dealer itself or its counterparty, or the agent of either the dealer or the counterparty, performed relevant security-based swap dealing activity within the United States.[101]

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98 See Cross-Border Proposing Release, 78 FR 31000-01.

99 See initially proposed 3a71-3(b)(1)(ii).

100 See initially proposed Exchange Act rule 3a71-3(a)(5). See also Cross-Border Proposing Release, 78 FR 30999-31000. To address anticipated operational challenges associated with determining whether a person's counterparty is engaging in dealing activity within the United States that would make the transaction a "transaction conducted within the United States," we also proposed permitting reliance on a representation by a counterparty that the transaction was not solicited, negotiated, executed, or booked within the United States by or on behalf of that counterparty. See id. at 31001.

101 As we noted in the Cross-Border Proposing Release, the term "transaction conducted within the United States" was intended to identify key aspects of a transaction that, if carried out within the United States by either counterparty, would trigger the need for a non-U.S. person acting in a dealing capacity to include transactions arising out of that activity in its de minimis calculation. See id. at 30999-31000. The initially proposed definition of "transaction conducted within the United States" did not include submitting a transaction for clearing in the United States, reporting a transaction to a security-based swap data repository in the United States, or performing collateral management activities (such as exchanging margin) within the United States. See id. at 31000.

2. Commenters' views on the Cross-Border Proposing Release

Our initially proposed definition of "transaction conducted within the United States" and our proposed use of that term to trigger various Title VII requirements generated a significant volume of comment addressing a wide range of issues. Although two commenters supported our proposal,[102] commenters generally criticized the proposed definition. These criticisms generally focused on four areas: the scope of activity potentially captured by the initially proposed defined term, the operational difficulties of implementing the defined term, the costs of implementation, and competitive concerns.

(a) Scope of the initially proposed definition of "transaction conducted within the United States"

Several commenters took issue with the scope of the initially proposed defined term. Some commenters argued that the initially proposed definition was inappropriate in the context of Title VII because it would capture transactions between two non-U.S. persons that happened to involve conduct within the United States, even though such transactions are unlikely to create risk to the U.S. financial system.[103] Commenters also expressed concern that the initially

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[102] See note 26, supra.

[103] See SIFMA/FIA/FSR Letter at 4, A-3 (explaining that a transaction between two non-U.S. counterparties does not create risk in the United States, even where it is conducted within the United States); Letter from European Commission ("EC") to SEC, dated August 21, 2013 ("EC Letter") at 2 (suggesting that the Commission's rules should not apply to transactions when conduct within the United States involves two non-U.S. counterparties because no U.S. firms are at risk); Letter from European Securities and Markets Authority ("ESMA") to SEC, dated August 21, 2013 ("ESMA Letter") at 2 (requesting the Commission limit the definition of "transaction conducted within the United States" to transactions booked within the United States because that is the only activity that directly creates risk within the United States); Letter from Futures and Options Association ("FOA") to SEC, dated August 21, 2013 ("FOA Letter") at 7 (arguing that the test as initially proposed does not serve the goals of preserving the integrity of U.S. financial markets and protecting U.S. counterparties because it reaches transactions with minimal nexus to the United States).

Two of these commenters suggested that the initially proposed approach exceeded the Commission's authority under section 30(c) of the Exchange Act. See SIFMA/FIA/FSR Letter at

proposed definition was overly broad because it would capture incidental or peripheral activity within the United States,[104] arguing that such overbreadth could lead to conflicting or duplicative application of regulations for certain market participants.[105]

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4 and A-4 to A-5 (suggesting that Exchange Act section 30(c) does not authorize the Commission to extend its authority through a conduct-based approach where no risk is imported to the United States); FOA Letter at 7 (stating that test goes beyond limits of Exchange Act section 30(c)). Another commenter stated that the initially proposed approach was inappropriate because it would have the effect of applying Title VII to transactions between two non-U.S. persons without having an international agreement regarding extraterritorial application of each jurisdiction's regulations. See Letter from Japan Securities Dealers Association ("JSDA") to SEC, dated August 21, 2013 ("JSDA Letter") at 3.

104 See Letter from Managed Funds Assoc. and Alternative Investment Management Assoc. ("MFA/AIMA") to SEC, dated August 19, 2013 ("MFA/AIMA Letter") at 4 and n.18 (stating that the lack of a materiality threshold would inappropriately subject transactions to Commission regulation, including transactions negotiated during an employee's visit to the United States); SIFMA/FIA/FSR Letter at A-2 (explaining that "transaction conducted within the United States" may include incidental conduct, which includes, in this commenter's view, a decision by a non-U.S. counterparty to use a contact based in the United States to execute a transaction only because executing it in the non-U.S. counterparties' jurisdictions would be inconvenient or impossible due to the timing of the transaction); Letter from Pensions Europe to SEC, dated September 3, 2013 ("Pensions Europe Letter") at 1 (stating that trades executed outside the United States by European pension fund managers should not be brought within Title VII only because the managers wish to "benefit from the expertise and experience of U.S. operations"); Letter from Institute of International Bankers ("IIB") to SEC, dated August 21, 2013 ("IIB Letter") at 10 (noting that the initially proposed test could capture transactions where the U.S.-based conduct is only clerical or ministerial); Letter from Investment Adviser Association ("IAA") to SEC, dated August 21, 2013 ("IAA Letter") at 6-7 (stating that the initially proposed test may capture parties with minimal connection to the United States, such as a non-U.S. counterparty using a U.S. investment adviser to manage its assets); Letter from Investment Company Institute ("ICI") to SEC, dated August 21, 2013 ("ICI Letter") at 4, 8-9 (stating that exception from the definition should be broader for non-U.S. counterparties that use U.S.-based investment managers and that the retention of a U.S. asset manager should not cause transactions to be subject to various regulatory requirements because a non-U.S. entity would not expect to be subject to U.S. regulation based on its retention of a U.S. asset manager); Letter from Japan Financial Markets Council ("JFMC") to SEC, dated August 15, 2013 ("JFMC Letter") at 5 (stating that the transactions could be captured by the definition solely because they are executed through a U.S. trading facility).

105 See IIB Letter at 8-9 (explaining that, because European regulations would apply to transactions between two U.S. branches of European firms, the initially proposed approach would cause duplicative and conflicting regulation); IIB letter at 10 (stating that a conduct-based test would subject U.S. agents already registered with the Commission or exempted from registration under broker-dealer or investment adviser regulations to additional regulation). See also EC Letter at 2 (suggesting that the Commission's rules should not apply to transactions when the legal counterparty to a transaction conducted within the United States is a non-U.S. entity because such

(b) Operational challenges

One commenter recognized the concerns that the initially proposed definition of "transaction conducted within the United States" was intended to address but expressed doubt as to whether funds would be able to monitor and confirm whether their dealing counterparties were engaging in dealing activity within the United States.[106] A number of commenters expressed concern that the defined term and its initially proposed application in the context of specific Title VII requirements, would present significant operational challenges for market participants more generally.[107] For example, one commenter noted that the approach would require market participants to make determinations on a trade-by-trade basis as to whether a transaction was "conducted within the United States" and would create inefficiencies and uncertainty in the market.[108] This commenter stated that the initially proposed approach was vague, and would be difficult to enforce and easy to manipulate.[109] One commenter specifically argued that

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persons are subject to regulation in their home jurisdiction); ESMA Letter at 2-3 (noting that the initially proposed approach could subject a transaction between two non-U.S. persons that is solicited in the United States to the regulations of multiple jurisdictions); FOA Letter at 7 (requesting that the Commission defer to regulatory oversight of counterparties' home country regulators).

106 See MFA/AIMA Letter at 4 (acknowledging the Commission's interest in preventing evasion of Title VII but expressing concern that private funds that are not U.S. persons may not be able to determine whether dealer counterparties have engaged in relevant conduct within the United States and may not be able to obtain relevant representations from such counterparties).

107 See, e.g., IIB Letter at 11 (stating that the initially proposed definition is ill suited to the global nature of the derivatives markets where activity may involve multiple physical locations); JFMC Letter at 4-5 (noting that the initially proposed definition is impracticable and would subject participants to duplicative and conflicting rules); JSDA Letter at 3 (expressing concern about the activity-based approach because of the operational confusion it may cause by subjecting market participants to the two separate approaches of the Commission and CFTC); ABA Letter at 3 (identifying ambiguities in the initially proposed definition, including whether negotiations over ISDA documentation are relevant conduct for purposes of the transaction).

108 See Letter from Americans for Financial Reform ("AFR") to SEC, dated August 22, 2013 ("AFR Letter") at 3, A-2 to A-3.

109 See AFR Letter at 3.

operational difficulties in tracking the location of conduct on a trade-by-trade basis might be impossible to overcome.[110]

(c) Cost concerns

Some commenters stated that applying Title VII to transactions merely because they involve conduct within the United States could not be justified from a cost-benefit perspective. Some contended that the CFTC had not taken such an approach and that divergence from the CFTC on the treatment of such conduct would impose a significant additional cost on market participants.[111] One commenter also noted that, whereas the "U.S. person" definition would typically be applied only at the beginning of a trading relationship, market participants would potentially be required to perform a trade-by-trade analysis to determine whether it involved conduct within the United States, which could significantly increase costs.[112]

(d) Competitive concerns

Some commenters expressed concern that focusing on "transactions conducted within the United States" would put brokers and investment managers located in the United States at a competitive disadvantage to their foreign counterparts, on the grounds that foreign clients would avoid doing business with them to avoid having their transactions become subject to

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110 See IIB Letter at 8.

111 See SIFMA/FIA/FSR Letter at 3, A-3, A-6 (arguing that the Commission should harmonize its approach to cross-border security-based swap activity to the approach reflected in the commenter's view of the CFTC Cross-Border Guidance); Pensions Europe Letter at 2 (preferring its view of the CFTC approach in the CFTC Cross-Border Guidance, which the commenter argues focuses on the location of principal headquarters); IIB Letter at 8 (stating that market participants would incur costs and burdens to modify their existing systems in order to comply with two different tests); JFMC Letter at 4-5 (urging that the Commission not adopt the defined term "transaction conducted within the United States" because the CFTC did not discuss such an approach in the CFTC Cross-Border Guidance).

112 See IIB Letter at 8 (stating that a conduct-based test would be costly and disruptive).

Commission regulations.[113] Another commenter, although critical of our initially proposed definition as excessively costly to implement, urged that any alternative to the conduct-based test described in the Cross-Border Proposal Release be designed to ensure that market participants from the United States were not put at a competitive disadvantage.[114]

(e) Other concerns

A few commenters, including some who expressed the concerns outlined above, sought clarification or made suggestions related to limiting the scope of the initially proposed defined term.[115] One commenter expressed support for the SEC's position in the proposal that the location where a transaction is cleared should not factor into determining whether a non-U.S. person qualifies as a security-based swap dealer.[116] Another commenter requested that, if the Commission adopts the "transaction conducted within the United States" test, market participants

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113 See IIB Letter at 8-9.

114 See SIFMA/FIA/FSR Letter at A-6.

115 See IIB Letter at 9-11 (requesting clarification as to what degree of solicitation, negotiation, or execution activity would trigger the initially proposed definition); ESMA Letter at 2-3 (inviting the Commission to clarify which transactions between a U.S. branch of a foreign firm would be considered "conducted within the United States" and arguing that location of booking alone should be considered); FOA Letter at 7 (suggesting that, if a transaction has more than a de minimis connection to the United States as a result of solicitation or negotiation in the United States, the Commission should focus its regulatory authority on the intermediary performing those activities); JSDA Letter at 3 (suggesting that the Commission limit the application of Title VII to those transactions booked by non-U.S. persons with U.S. persons and requesting that certain activity related to "operational activities" be excluded from the activity covered by the initially proposed definition); ABA Letter at 3-4 (supporting the initially proposed definition but suggesting clarification that it excludes a firm's centralized risk management and legal and compliance functions).

116 See Letter from CME Group ("CME") to SEC, dated August 21, 2013 ("CME Letter") at 2 (citing Cross-Border Proposing Release, 78 FR 31000).

should be permitted to rely on their counterparties' representations as to whether the transaction was conducted within the United States.[117]

3. The CFTC Staff Advisory and responses to the CFTC Request for Comment

As already noted, in November 2013, subsequent to the close of the comment period for our Cross-Border Proposing Release, CFTC staff issued the CFTC Staff Advisory, which addressed activity by registered swap dealers occurring within the United States.[118] The CFTC Staff Advisory stated the CFTC staff's belief that the CFTC "has a strong supervisory interest in swap dealing activities that occur within the United States, regardless of the status of the counterparties" and that a non-U.S. swap dealer "regularly using personnel or agents located in the U.S. to arrange, negotiate, or execute a swap with a non-U.S. person generally would be required to comply with" the CFTC's transaction-level requirements.[119]

As noted above, on January 8, 2014, the CFTC published the CFTC Request for Comment on various aspects of the CFTC Staff Advisory, including whether the CFTC "should adopt the Staff Advisory as Commission policy, in whole or in part."[120] In response to this request, the CFTC received approximately 20 comment letters addressing various aspects of the CFTC Staff Advisory, including its relationship to the CFTC Cross-Border Guidance and its general workability given current market practices. CFTC staff subsequently extended no-action relief related to the CFTC Staff Advisory until the earlier of September 30, 2015, or the effective

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117 See JSDA Letter at 4. Another commenter, however, expressed concern about being able to obtain, and being able to confirm the accuracy of, such representations. See MFA/AIMA Letter at 4.

118 See CFTC Staff Advisory.

119 Id. at 2.

120 See CFTC Request for Comment, 79 FR 1347.

date of any CFTC action in response to the CFTC Request for Comment.[121] We understand that the CFTC Staff Advisory and the related comment letters are currently under review by the CFTC. Although the CFTC Staff Advisory raises issues that are, to a certain degree, distinct from those raised by our initially proposed definition and use of "transaction conducted within the United States," the comments received by the CFTC in response to the CFTC Request for Comment in many cases elaborate on issues that commenters raised in response to our Cross-Border Proposing Release. Given similarities between the approach set forth in the CFTC Staff Advisory and our proposed amendments identifying relevant conduct within the United States, in this section we provide our own brief summary of relevant comments received by the CFTC.[122]

A few commenters supported the CFTC Staff Advisory. One commenter urged the CFTC to formally adopt the approach in the CFTC Staff Advisory, arguing that any weakening of it would permit "nominally foreign entities" to do business within the United States in compliance with foreign laws and regulations, or potentially subject to no legal requirements, rather than with U.S. law.[123] Another commenter stated that formal adoption of the CFTC Staff Advisory was unnecessary but urged the CFTC to leave it undisturbed, arguing that without the CFTC Staff Advisory, a U.S. person would effectively be able to enter into transactions with

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[121] See note 25, supra.

[122] As reflected in our discussion throughout this release, we have carefully considered both the CFTC Staff Advisory and the comments submitted in response to the CFTC's request for comment on the CFTC Staff Advisory in developing this proposal. Moreover, in connection with our statutory obligation to consult with the CFTC in connection with Title VII rulemaking, our staff have engaged in extensive discussion with CFTC staff regarding our proposed rules. We note, however, that our discussion of both the CFTC Staff Advisory and the comments received by the CFTC about it reflects our understanding of these documents. Accordingly, neither our discussions of these documents nor any preliminary views expressed herein should be interpreted as necessarily reflecting the views of any other agency or regulator, including the CFTC.

[123] See Letter from American for Financial Reform ("AFR") to CFTC, dated March 10, 2014 ("AFR Letter to CFTC") at 3-4. See also Letter from Institute for Agriculture and Trade Policy ("IATP") to CFTC, dated March 10, 2014 ("IATP Letter to CFTC") at 1-2.

non-U.S. persons through its foreign affiliates while using U.S.-based trading operations, "thereby evading and gutting the key components of financial reform."[124]

Most commenters, however, opposed the approach taken in the CFTC Staff Advisory. These commenters expressed several concerns that may also be relevant to our own proposal to impose certain Title VII requirements on security-based swap activity that is carried out from a U.S. location, including the following: (1) the scope of the activity that would trigger application of Title VII, (2) the workability and costs of complying with such a test and resulting effects on competition and comity, and (3) the CFTC's transaction-level requirements that should be triggered by such a test. We will discuss the first two sets of concerns here and the third in Section V below.

(a) Scope of the CFTC Staff Advisory

Several commenters argued that the scope and types of activity by non-U.S. swap dealers captured by the CFTC Staff Advisory were unclear. The CFTC Staff Advisory notes that "persons regularly arranging, negotiating, or executing swaps for or on behalf of [a swap dealer] are performing core, front-office activities of that [swap dealer's] dealing business."[125] Accordingly, it expresses the CFTC staff's view that the CFTC's transaction-level requirements apply to transactions of registered non-U.S. swap dealers with non-U.S.-person counterparties when they "arrange, negotiate, or execute" those transactions "using personnel or agents located in the U.S."[126] Commenters argued that "arrange" and "negotiate" were overly broad and could

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124 Letter from Better Markets to CFTC, dated March 10, 2014 ("Better Markets Letter to CFTC") at 6.

125 CFTC Staff Advisory at 2.

126 Id.

encompass activity that occurred only incidentally in the United States.[127] Some commenters also noted that the apparent scope of the CFTC Staff Advisory was overly broad because non-U.S.-person counterparties may not typically know where the dealer engages in relevant conduct with respect to a particular swap transaction.[128]

Some commenters encouraged the CFTC to address these concerns by providing "detailed definitions" of the relevant terms or to focus only on execution or other discrete activities related to the transaction.[129] Several commenters urged the CFTC to abandon the CFTC Staff Advisory's approach altogether, or, if not, to revise the CFTC Staff Advisory's approach to focus on activities involving direct communication with the counterparty to the swap.[130]

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127 See, e.g., Letter from Investment Adviser Association to CFTC, dated March 10, 2014 ("IAA Letter to CFTC") at 5; Société Générale Letter to CFTC at 7-8 (arguing that key terms of CFTC Staff Advisory are ambiguous and do not reflect how swap business is carried out). Some commenters also raised concerns regarding ambiguity in the CFTC Staff Advisory's use of the term "regularly." See, e.g., Letter from Securities Industry and Financial Markets Association/Futures Industry Association/Financial Services Roundtable to CFTC, dated March 10, 2014 ("SIFMA/FIA/FSR Letter to CFTC") at 16.

128 See, e.g., Letter from Société Générale to CFTC, dated March 10, 2014 ("Société Générale Letter to CFTC") at 8 (stating that "[m]ost clients have no control or knowledge over where their swap is structured or designed, where the salesperson responsible for a particular product is located, where the booking of their swap is entered into a trading system, or where their swap is hedged").

129 See, e.g., Letter from European Commission to CFTC, received March 10, 2014 ("EC Letter to CFTC") at 3. See also SIFMA/FIA/FSR Letter to CFTC at A-8 to A-9; IAA Letter to CFTC at 5 (urging CFTC to focus on where the swap was executed or cleared).

130 See Letter from ISDA to CFTC, dated March 7, 2014 ("ISDA Letter to CFTC") at 8 n.16 (arguing that, if the CFTC determines to adopt the CFTC Staff Advisory, it should limit triggering conduct solely to "direct communications by SD personnel located in the United States with counterparties, which communications commit the SD to the execution of a particular swap transaction"); Letter from Barclays to CFTC, dated March 10, 2014 ("Barclays Letter to CFTC") at 4 (arguing that "only direct communication with counterparties by non-U.S. swap dealers to the execution of the transaction should trigger application of the pre-trade disclosure requirements" and that "the [CFTC] should explicitly exclude electronic or screen-based execution" as such conduct "does not involve direct interaction" and the "non-U.S. person counterparty will not know who is responding on behalf of the non-U.S. swap dealer, let alone the responder's location," meaning that "the non-U.S. counterparty will not have a reasonable expectation that the

(b) Workability, costs, and competitive effects of the CFTC's activity-based approach

Some commenters expressed concern that the CFTC Staff Advisory reflected a significant departure from the approach that these commenters understood to be the focus of the CFTC Cross-Border Guidance.[131] These commenters argued that developing systems consistent with the CFTC Staff Advisory would cause them to incur significant additional costs.[132] In particular, commenters stated their belief that developing systems consistent with the CFTC Staff Advisory would require a trade-by-trade analysis, which would be impracticable.[133] One commenter argued that these costs would not be justified by corresponding benefits because

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transaction may be subject to protection under U.S. law"); SIFMA/FIA/FSR Letter to CFTC at A-11 to A-12 (arguing that, if the CFTC decides to adopt the approach in the CFTC Staff Advisory, it should capture only "direct communications by personnel in the United States with counterparties that commit the SD to the execution of the transaction" because, absent direct communication, the counterparty has no reason to expect that U.S. law will apply to the transaction). See also Société Générale Letter to CFTC at 8 (stating that, if the CFTC does adopt the CFTC Staff Advisory, the CFTC should focus only on salespersons based in the United States that deal directly with clients).

131 See Société Générale Letter to CFTC at 2 (explaining that market participants have already developed systems to reflect the status-based approach); Letter from Institute of International Bankers to CFTC, dated March 10, 2014 ("IIB Letter to CFTC") at 2-3 (noting among other things that market participants have built policies and systems to reflect their view of the CFTC's approach in the CFTC Cross-Border Guidance and that they believe the approach taken in the CFTC Staff Advisory is fundamentally different); ISDA Letter to CFTC at 5 (arguing that systems are not configured to identify personnel that are involved in a transaction but rather to be consistent with the CFTC Cross-Border Guidance, and that the CFTC Staff Advisory raises complex questions about, e.g., portfolio margining); SIFMA/FIA/FSR Letter to CFTC at A-2 (stating that the CFTC's approach in the CFTC Cross-Border Guidance is already overbroad, and applying the CFTC Staff Advisory on top of the entity-based approach is "particularly flawed," "compound[ing] the excessive breadth and burden of the existing, entity-based regulatory structure by approaching swaps regulation from an entirely different direction, layering even more requirements and burdens onto market participants, and doing so in the absence of any discernible risk to U.S. markets").

132 See, e.g., Société Générale Letter to CFTC at 2.

133 See, e.g., Société Générale Letter to CFTC at 8; SIFMA/FIA/FSR Letter to CFTC at A-4 (explaining that the approach taken in the CFTC Staff Advisory is impracticable in the swap market, as it would require a trade-by-trade analysis that is not feasible and that requiring such trades to be fully isolated from the United States would interfere with the operations of these markets and market participants).

market participants likely would already be subject to similar requirements in their home jurisdiction.[134]

One commenter criticized the CFTC Staff Advisory's focus on whether a registered non-U.S. swap dealer is arranging, negotiating, or executing a swap using personnel or agents in the United States as providing insufficient guidance to market participants, arguing that these activities do not reflect current business practices among swap dealers.[135] For example, this commenter stated that some personnel of a dealer may design swaps and hedging solutions but lack authority to book the resulting swaps and have no interaction with clients; these same personnel may book swaps that other employees have sold or negotiated for risk mitigation purposes.[136] The commenter further noted that personnel involved in a particular swap may be located in multiple jurisdictions.[137]

Several commenters argued that the costs and impracticability of the approach taken in the CFTC Staff Advisory would have competitive effects, although they disagreed whether it would enhance or degrade competition. One commenter supported the CFTC Staff Advisory in its current form, noting that without it, U.S. firms would be at a competitive disadvantage compared to non-U.S. firms operating in the United States.[138] Other commenters argued that the

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134 See IIB Letter to CFTC at 3.

135 See Société Générale Letter to CFTC at 8.

136 See id.

137 See id.

138 See AFR Letter to CFTC at 3 (explaining that "any weakening of [the] advisory would open the door to regular and significant levels of swaps activities being performed within the U.S. by nominally foreign entities under foreign rules, or in some cases no rules at all," whereas U.S. firms operating in the United States would be subject to different rules for the same transactions operating in the same market).

CFTC Staff Advisory, if adopted, would have adverse competitive effects on certain end users.[139]

Some commenters also suggested that, if adopted by the CFTC, the approach taken in the CFTC Staff Advisory could present difficulties for, and impose costs on, non-U.S.-person counterparties of dealers, as such counterparties may not currently have systems in place for complying with certain CFTC requirements, particularly if they are imposed only because the swap dealer (and not the counterparty) happens to have carried out certain activities using personnel or agents located in the United States.[140] As a result, commenters argued non-U.S. swap dealers may no longer service non-U.S.-person counterparties from U.S. locations.[141]

Commenters suggested that pressure from non-U.S.-person counterparties that do not want their transactions to be subject to Title VII would lead at least some non-U.S.-person dealers to exit the United States.[142] Commenters suggested that the adoption of the CFTC Staff Advisory would likely interfere with the ability of certain swap dealers to cover U.S. market hours for foreign counterparties with U.S.-based personnel, increasing costs to counterparties and end users.[143]

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139 See Letter from Coalition for Derivatives End-Users ("CDEU") to CFTC, dated March 10, 2014 ("CDEU Letter to CFTC") at 2 (arguing that the CFTC Staff Advisory would lead to competitive disadvantages for certain non-U.S. end-user affiliates that had relied on trading with non-U.S. swap dealers compared to other non-U.S. end users in the same markets that currently hedge with unregistered counterparties).

140 See, e.g., SIFMA/FIA/FSR Letter to CFTC at A-4 (explaining that certain non-U.S.-person counterparties may not have a clearing relationship with a futures commission merchant ("FCM"), and requiring them to clear through an FCM simply because the dealer happens to use personnel within the United States in the transaction will be costly).

141 See ISDA Letter to CFTC at 4.

142 See, e.g., Société Générale Letter to CFTC at 8 (stating that, if the CFTC adopts the CFTC Staff Advisory, or even an alternative suggested by the commenter, swap dealers "will move personnel currently based in the United States offshore").

143 See, e.g., Letter from Paul Hunter for the Japan Financial Markets Council to CFTC, dated March 4, 2014 ("JFMC Letter to CFTC") at 1-2 (explaining that the approach in the CFTC Staff Advisory "unfairly precludes options open to Asia-based Swap Dealers to cover U.S. market

4. Dealing activity of non-U.S. persons in the United States

We have carefully considered the views of commenters, as discussed above, that dealing activity carried out in the United States by a non-U.S. person with a counterparty that is also a non-U.S. person lacks a significant nexus to the United States and does not raise any significant regulatory concerns in the United States because the ongoing obligations associated with such transactions do not reside in the United States.[144] However, as we discuss below, we continue to believe that such activity falls squarely within our territorial approach to the application of Title VII[145] and that it raises regulatory concerns of the type that Title VII addresses.

(a) Overview of common business structures for firms engaged in security-based swap dealing activity

As we noted in our Cross-Border Proposing Release, financial groups engaged in security-based swap dealing activity use a variety of business models and legal structures to carry out such activity with counterparties around the world. Most such financial groups operate in multiple jurisdictions, and they will typically have one or more dealer affiliates in one or more

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hours and service their non-U.S. based clients by using U.S.-based personnel or agents"); CDEU Letter to CFTC at 2-3 (arguing that the CFTC Staff Advisory's approach would "force non-U.S. [swap dealers] that use personnel or agents to 'arrange, negotiate, or execute' swaps to exit certain markets or move personnel outside the U.S. in order to remain competitive in non-U.S. markets[,]" and that the costs associated with such movements would "undoubtedly be passed on to derivatives end-users and ultimately to customers…[which] would result in a loss of liquidity that will leave non-U.S. end-user affiliates scrambling to find counterparties to hedge their risks"). See also SIFMA/FIA/FSR Letter to CFTC at A-6 (explaining that the desire of counterparties to swap dealers to keep their transactions out of the reach of Dodd-Frank will lead them to pressure non-U.S.-person dealers and foreign branches to move personnel out of the United States); IAA Letter to CFTC at 3 (explaining that non-U.S.-person dealers may incur expenses associated with moving personnel out of the United States or hiring personnel in other jurisdictions, which may potentially lead to increased transaction costs and reduced services for advisers' non-U.S. clients, and that these higher costs may drive non-U.S. clients away from U.S. investment advisers).

144 See note 103, supra (identifying comment letters arguing that such transactions pose no risk to the United States or that the Commission lacks a regulatory interest in such transactions).

145 See Cross-Border Proposing Release, 78 FR 30986; Cross-Border Adopting Release, 79 FR 47290.

jurisdictions that book the security-based swap transactions related to their security-based swap dealing business. An affiliate that initially books a transaction may retain the risk associated with that transaction, or it may lay off that risk to another affiliate via a back-to-back transaction or an assignment of the security-based swap.[146] These decisions generally reflect the financial group's consideration of, among other things, how it may most efficiently manage the risks associated with its security-based swap positions.

The structure of the group's market-facing activities that generate the transactions booked in these affiliates often reflects different considerations. A dealing affiliate established in one jurisdiction may operate offices (which may serve sales or trading functions) in one or more other jurisdictions to deal with counterparties in that jurisdiction or in a specific geographic region, or to ensure that it is able to provide liquidity to counterparties in other jurisdictions, even when a counterparty's home financial markets are closed. A dealer also may choose to manage its trading book in particular reference entities or securities primarily from a trading desk that can take advantage of local expertise in such products or to gain access to better liquidity, which may permit it to more efficiently price such products or to otherwise compete more effectively in the security-based swap market. We understand that a financial group that engages in a dealing business may have business lines that are carried out in a number of affiliates located in different jurisdictions, and that personnel of an affiliate may operate under the direction of, or in some cases, report to personnel of another affiliate within the group; in some cases, such personnel work on behalf of, or under the supervision of, more than one affiliate in the group.

Moreover, a dealer may carry out these market-facing activities, whether in its home jurisdiction or in a foreign jurisdiction, using either its own personnel or the personnel of an

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[146] See Cross-Border Proposing Release, 78 FR 30977-978.

affiliated or unaffiliated agent. For example, the dealer may determine that another affiliate in the financial group employs personnel who possess expertise in relevant products or that have established sales relationships with key counterparties in a foreign jurisdiction, making it more efficient to use the personnel of the affiliate to engage in security-based swap dealing activity on its behalf in that jurisdiction.

Alternatively, the dealer may in some circumstances determine to engage the services of an unaffiliated agent through which it can engage in dealing activity. For example, a dealer may determine that using an inter-dealer broker may provide an efficient means of participating in the inter-dealer market in its own, or in another, jurisdiction, particularly if it is seeking to do so anonymously or to take a position in products that trade relatively infrequently.[147] Dealers may also use unaffiliated agents that operate at the direction or request of the dealer to engage in dealing activity. Such arrangement may be particularly valuable in enabling the dealer to service clients or access liquidity in jurisdictions in which the dealer or its affiliates have no security-based swap operations of their own.

We understand that dealers established in foreign jurisdictions (whether affiliated with U.S.-based financial groups or not) may use any of these structures to engage in dealing activity in the United States, and that they may seek to engage in dealing activity in the United States to transact with both U.S. and non-U.S.-person counterparties. In transactions with non-U.S.-person counterparties, a foreign dealer may affirmatively seek to engage in dealing activity in the United States because the sales personnel of the foreign dealer (or of its agent) in the United

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[147] We understand that inter-dealer brokers may provide voice or electronic trading services that, among other things, permit dealers to take positions or hedge risks in a manner that preserves their anonymity until the trade is executed. These inter-dealer brokers also may play a particularly important role in facilitating transactions in less-liquid security-based swaps.

States have existing relationships with counterparties in other locations (such as Canada or Latin America) or because the trading personnel of the foreign dealer (or of its agent) in the United States have the expertise to manage the trading books for security-based swaps on U.S. reference securities or entities. And we understand that some foreign dealers engage in dealing activity in the United States through their personnel (or personnel of their affiliates) in part to ensure that they are able to provide their own counterparties, or those of financial group affiliates in other jurisdictions, with access to liquidity (often in non-U.S. reference entities) during U.S. business hours, permitting them to meet client demand even when the home markets are closed. In some cases, such as when seeking to transact with other dealers through an inter-dealer broker, a foreign dealer may act, in a dealing capacity, in the United States through an unaffiliated, third-party agent.

(b) Statutory scope and policy concerns arising from security-based swap dealing activity in the United States

As discussed above, some commenters have suggested that the Title VII statutory framework does not extend to transactions between two non-U.S. persons, even if security-based swap activity occurs in the United States, and have argued that section 30(c) of the Exchange Act limits our authority to reach this conduct.[148] We continue to believe, however, that it is consistent with the Exchange Act to impose specific Title VII requirements on non-U.S. persons that engage in activity within the United States that is regulated by the relevant statutory provision.[149]

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148 See note 103, supra.

149 See Cross-Border Adopting Release, 79 FR 47287. As we noted in the Cross-Border Adopting Release, when the statutory text does not describe the relevant activity with specificity or provides for further Commission interpretation of statutory terms or requirements, our territorial analysis may require us to identify through interpretation of the statutory text the specific activity

In the Cross-Border Adopting release, we described how this approach applies in the specific context of the definition of "security-based swap dealer." We rejected the view that "the location of risk alone should . . . determine the scope of an appropriate territorial application of every Title VII requirement," including the application of the "security-based swap dealer" definition.[150] In doing so, we noted that "neither the statutory definition of 'security-based swap dealer,' our subsequent further definition of the term pursuant to section 712(d) of the Dodd-Frank Act, nor the regulatory requirements applicable to security-based swap dealers focus solely on risk to the U.S. financial system."[151]

Instead, the statute identifies specific activities that bring a person within the definition of "security-based swap dealer": (1) holding oneself out as a dealer in security-based swaps, (2) making a market in security-based swaps; (3) regularly entering into security-based swaps with counterparties as an ordinary course of business for one's own account; or (4) engaging in any activity causing oneself to be commonly known in the trade as a dealer in security-based swaps.[152] We have further interpreted this definition to apply to persons engaged in indicia of dealing activity, including, among other things, providing liquidity to market professionals, providing advice in connection with security-based swaps, having regular clientele and actively soliciting clients, and using inter-dealer brokers.[153] Neither the statutory definition of "security-

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that is relevant under the statute or to incorporate prior interpretations of the relevant statutory text. See id.

150 Id. at 47287-88.

151 Id. at 47288. We have also noted that security-based swap dealer regulation may be warranted either to promote market stability and transparency in light of the role that these dealers occupy in the security-based swap market or to address concerns raised by the nature of the interactions between such dealers and their counterparties. See Intermediary Definitions Adopting Release, 77 FR 30617.

152 See Exchange Act section 3(a)(71)(A), 15 U.S.C. 78c(a)(71)(A).

153 See Intermediary Definitions Adopting Release, 77 FR 30617-18.

based swap dealer" nor our further definition of that term turns primarily on the presence of risk or on the purchase or sale of any security, including a security-based swap.[154]

Accordingly, the fact that the counterparty credit risk from a transaction between two non-U.S. persons, where neither counterparty has a right of recourse against a U.S. person under the security-based swap, exists largely outside the United States is not determinative under our territorial analysis. The appropriate analysis, in our view, is whether a non-U.S. person in such a transaction is engaged, in the United States, in any of the activities set forth in the statutory definition or in our further definition of "security-based swap dealer." If it is so engaged, in our view, it is appropriate under a territorial approach to require the non-U.S. person to include such transaction in its security-based swap dealer de minimis threshold calculations and, if those security-based swaps (and any other security-based swaps it is required to include in its threshold calculations) exceed the de minimis threshold, to register as a security-based swap dealer.[155]

This analysis applies regardless of whether the non-U.S. person engages in dealing activity (as described in the statutory definition and in our further definition of "security-based swap dealers") in the United States using its own personnel or using the personnel of an agent acting on its behalf. As described above, persons engaged in security-based swap dealing activity routinely do so both directly and through their agents. Indeed, our further definition of

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154 See Exchange Act section 3(a)(71)(A), 15 U.S.C. 78c(a)(71)(A); Intermediary Definitions Adopting Release, 77 FR 30617-18.

155 See Cross-Border Adopting Release, 79 FR 47286-92 (describing the Commission's territorial approach). We note that another commenter argued that it was inappropriate to use activity in the United States to trigger application of Title VII absent an international agreement between regulators. See note 103, supra. As discussed above, we have continued to consult and coordinate with other regulators in the United States and abroad in connection with financial market reforms, see note 12 and accompanying discussion, but we do not believe that an international agreement is relevant as a legal or policy matter in determining whether to impose Title VII requirements on security-based swap activity, particularly given that we are proposing to do so with respect to activity that is being carried out in the United States.

"security-based swap dealer" specifically identifies the use of inter-dealer brokers as one of several indicia of security-based swap dealing activity,[156] and, in our preliminary view, engaging an inter-dealer broker as agent or sending a trade to such a broker generally would be dealing activity; to the extent that this activity is directed to a broker in the United States, we preliminarily believe that the non-U.S. person would be engaged in dealing activity in the United States.[157] Accordingly, a non-U.S. person that reaches into the United States by engaging an agent (including an inter-dealer broker) to perform dealing activity on its behalf is itself engaged, at least in part, in dealing activity in the United States. We preliminarily believe that it is appropriate under a territorial approach to require the non-U.S. person to include transactions arising out of those activities in its own de minimis threshold calculations.

Finally, in light of the foregoing analysis, we note that the statutory prohibition on application of Title VII requirements to persons that "transact[] a business in security-based swaps without the jurisdiction of the United States" has no bearing on these proposed rules.[158] Our proposed approach, as described in further detail below, would require transactions to be included in a non-U.S. person's dealer de minimis threshold calculations only when, in connection with its dealing activity, it arranges, negotiates, or executes a security-based swap using its personnel (or personnel of its agent) located in the United States.[159] Because we are

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156 See Intermediary Definitions Adopting Release, 77 FR 30617-18 (further defining "security-based swap dealer").

157 More generally, we note that the routine use by dealers of the structures described in this discussion suggest that a person may engage in dealing activity through an agent in a manner very similar to such activity carried out through its own branch or office. Cf. Exchange Act section 3(a)(71)(A) (defining "security-based swap dealer"); Intermediary Definitions Adopting Release, 77 FR 30617-18 (further defining "security-based swap dealer").

158 See Exchange Act section 30(c).

159 See Exchange Act rule 3a71-3(a)(1).

focusing in this proposal solely on transactions in which the non-U.S. person is engaged, directly or indirectly, in dealing activity in the United States, the proposed rules would not impose requirements on non-U.S. persons that are "transacting a business in security-based swaps without the jurisdiction of the United States" for purposes of section 30(c).[160] Accordingly, because such activities occur within the United States, they, and any resulting transaction, are within the scope of Title VII.

Moreover, we preliminarily believe that requiring these transactions to be included in a non-U.S. person's dealer de minimis threshold calculations (and subjecting them to certain other Title VII requirements, as discussed below) is consistent with the regulatory objectives furthered by the relevant Title VII requirements. Under the rules we adopted in the Cross-Border Adopting Release, financial groups may seek to avoid application of Title VII requirements to their security-based swap dealing activity with non-U.S. persons (including with other dealers),

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[160] As noted above, we do not believe that our proposed approach applies Title VII to persons that are "transact[ing] a business in security-based swaps without the jurisdiction of the United States," within the meaning of section 30(c) of the Exchange Act. An approach that, for example, treated a non-U.S. person dealer that used an agent, whether affiliated or unaffiliated, in the United States to carry out some or all of its dealing business with non-U.S. persons (for example, because using a U.S. agent allowed it to leverage higher liquidity and lower spreads in U.S. reference entities) as transacting a business in security-based swaps without the jurisdiction of the United States, would, in our view, reflect an understanding of what it means to conduct a security-based swaps business within the jurisdiction of the United States that is divorced both from Title VII's statutory objectives and from the various structures that non-U.S. persons use to engage in security-based swap dealing activity. But in any event we also preliminarily believe that this proposed rule is necessary or appropriate as a prophylactic measure to help prevent the evasion of the provisions of the Exchange Act that were added by the Dodd-Frank Act, and thus would help prevent the relevant purposes of the Dodd-Frank Act from being undermined. See Cross-Border Adopting Release, 79 FR 47291-92 (interpreting anti-evasion provisions of Exchange Act section 30(c)). Without this rule, non-U.S. persons could simply carry on a dealing business within the United States with other non-U.S. persons through agents and remain outside of the application of the dealer requirements of Title VII. Permitting this activity would allow these firms to retain full access to the benefits of operating in the United States while avoiding compliance with, for example, recordkeeping and reporting requirements and Regulation SBSR, which could reduce transparency in the U.S. market and make it considerably more difficult for the Commission to monitor the market for manipulation or other abusive practices.

even though they continue to carry out day-to-day sales and trading operations in the United States in a manner largely unchanged from what we understand to be current business practices.[161] For market participants, avoiding Title VII in such transactions in the absence of these proposed rules would require them only to book any such transactions in non-U.S. person dealers whose obligations under such swaps are not guaranteed by a U.S. person. Doing so would allow them to perform any other activities in connection with the transaction in the United States without complying with Title VII requirements.

Such a reaction could result in a significant amount of security-based swap dealing activity continuing to be engaged in by personnel located in a U.S. branch or office,[162] but, because the financial group chooses to book the transactions in a non-U.S.-person affiliate whose obligations under a security-based swap are not guaranteed by a U.S. person, certain Title VII requirements may not apply to such dealing activity. A dealer could continue to transact security-based swaps with other dealers (and with non-U.S. persons that are not dealers) through a U.S. sales and trading desk that is staffed by its own personnel or the personnel of its agent, continuing to engage in market-facing activity in the United States without complying with any Title VII requirements.

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161 We understand that there may be significant advantages in continuing to carry out certain market-facing activities using personnel located in the United States, depending on the location of the counterparty and the nature of the reference security or entity. For example, market expertise in security-based swaps on U.S. reference entities may be located primarily in the United States, and relationships with counterparties in certain geographical regions may be managed out of a U.S. branch or office. See Section III.B.4(a), supra.

162 This dealing activity likely would constitute inter-dealer activity, which, as noted above, accounts for a majority of activity in the security-based swap market. See Section II.B.2, supra. To the extent that there are advantages to trading U.S. reference entities from a U.S. location, activity by personnel located in the United States may account for a significant proportion of the inter-dealer business on those reference entities.

Although such transactions may not give rise to counterparty-credit risk within the United States, they do raise other regulatory concerns, particularly when a firm is engaged in such activity at levels above the dealer de minimis thresholds. We note that significant levels of security-based swap dealing activity occurring within the United States without being subject to dealer regulation or Regulation SBSR may pose a risk to the integrity of the U.S. financial market, as the absence of regulation—and of access, for example, to the security-based swap dealer's books and records—may make it significantly more difficult for the Commission to monitor the market for abusive and manipulative practices connected with security-based swap activity in the United States. As we have noted elsewhere, Title VII recordkeeping requirements will likely be the Commission's primary tool in monitoring compliance with applicable securities laws, including the antifraud provisions of these laws.[163] To the extent that we do not have access to reports of such transactions available through registered SDRs or to the books and records of non-U.S.-person dealers using personnel located in a U.S. branch or office, manipulative or abusive trading practices within the United States are more likely to go undetected, which may undermine the integrity of the security-based swap market in the United States, and of the U.S. financial market more generally.[164] For example, a dealer using personnel located in a U.S. branch or office may employ a trader who engages in trading practices in

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[163] See Requirements for Security-Based Swap Dealers, Major Security-Based Swap Participants, and Broker-Dealers; Capital Rule for Certain SBSDs; Proposed Rules, Exchange Act Release No. 71958 (April 17, 2014), 79 FR 25194, 25199 (May 2, 2014) (citing Commission Guidance to Broker-Dealers on the Use of Electronic Storage Media under the Electronic Signatures in Global and National Commerce Act of 2000 with Respect to Rule 17a–4(f), Exchange Act Release No. 44238 (May 1, 2001), 66 FR 22916 (May 7, 2001); Books and Records Requirements for Brokers and Dealers Under the Securities Exchange Act of 1934, Exchange Act Release No. 44992 (October 26, 2001), 66 FR 55818 (November 2, 2001)).

[164] These concerns may arise whether the dealer is using its own personnel or personnel of an affiliated or unaffiliated agent. For example, a security-based swap dealer may provide its agent's personnel located in a U.S. branch or office with false or misleading information concerning the transaction, which the agent's personnel then may deliver to the counterparty.

connection with security-based swap transactions that render the dealing activity in the United States abusive or manipulative, but we may not be able to readily identify the abusive or manipulative nature of that dealing activity without access to the dealer's books and records.[165] Detecting misconduct may be particularly challenging if a significant proportion of transactions in the relevant security-based swaps are carried out in the United States by traders employed by unregistered dealers.

Moreover, these dealers could continue to trade—using U.S. sales and trading desks, and potentially the same sales and trading desks used by their registered security-based swap dealer affiliates—in the inter-dealer market in a manner that may be opaque to regulators and non-dealers alike. This risk, in our preliminary view, is particularly high given that, as we have noted, inter-dealer activity accounts for a significant proportion of all security-based swap activity. This activity, to the extent it is carried out by personnel located in the United States, should be subject to relevant regulatory requirements. Subjecting such transactions to Regulation SBSR and potentially requiring firms engaged in such activity to register as security-based swap dealers should bring additional transparency to what is likely to be a significant proportion of the security-based swap activity that occurs in the United States and provide market participants more confidence in the integrity of the market.

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[165] A registered security-based swap dealer that is engaged in abusive or manipulative conduct with respect to a series of transactions may lay off risk from a transaction with a U.S. person counterparty to a foreign unregistered dealer via an affiliated foreign unregistered dealer, using personnel located in a U.S. branch or office. This conduct may not be apparent from the U.S. counterparty-facing leg or the inter-affiliate leg. Thus, even if the affiliated or unaffiliated agent has independent obligations arising from its role in the transaction, these obligations may not address potential abusive or manipulative practices in the transactions. Moreover, detecting such misconduct on the part of the affiliated foreign unregistered dealer, as discussed above, may be difficult absent access to regulatory reports of the relevant transactions and to the books and records of such dealer.

In light of these concerns, we preliminarily believe that it is appropriate to propose rules that would impose certain Title VII requirements on dealers using personnel located in the United States to engage in security-based swap dealing activity.

5. Proposed amendments regarding application of the dealer de minimis exception to non-U.S. persons using personnel located in a U.S. branch or office to arrange, negotiate, or execute security-based swap transactions

We have carefully considered the proposed application of the dealer de minimis exception to "transactions conducted within the United States" in light of comments received on the proposal, subsequent regulatory and other developments in the security-based swap market, and the policy concerns described in the preceding section. As a result, we are proposing an amendment to Exchange Act rule 3a71-3 that should address the regulatory concerns raised by dealing activity carried out using personnel located in the United States while mitigating many of the concerns expressed by commenters. Under this modified approach, we focus on market-facing activity by personnel located in the United States that reflects, in our view, a dealer's determination to engage in dealing activity in the United States in a manner that warrants, if the dealer exceeds the security-based swap dealer de minimis thresholds, application of Title VII security-based swap dealer regulation.

Unlike the initial proposal, which included the defined term "transaction conducted within the United States," the proposed amendment would not include a separate defined term identifying such activity. Rather, we propose to amend Exchange Act rule 3a71-3(b)(1)(iii) to require a non-U.S. person engaged in security-based swap dealing activity to include in its de minimis calculations any transactions connected with its security-based swap dealing activity that it arranges, negotiates, or executes using its personnel located in a U.S. branch or office, or

using personnel of its agent located in a U.S. branch or office.[166] To the extent that a non-U.S. person, in connection with its dealing activity, engages in market-facing activity using personnel located in the United States, we preliminarily believe that it is reasonable to conclude that the person is performing activities that fall within the statutory definition of "security-based swap dealer" or our further definition of that term, as described above, at least in part in the United States.[167]

This proposed amendment reflects our reconsideration of the issues raised by security-based swap dealing activity involving two non-U.S. persons in which one or both parties, or the agents of one or both parties, using personnel located in the United States, engage in some dealing activity.[168] We preliminarily believe that requiring non-U.S. persons to include such transactions in their de minimis threshold calculations will help to ensure that all persons that

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166 See proposed Exchange Act rule 3a71-3(b)(1)(iii)(C). Because, as a threshold matter, a person would be required to include in its de minimis calculations only security-based swaps that are arranged, negotiated, or executed in connection with its dealing activity, a non-U.S. person would not be required to include in this calculation transactions solely on the basis that they were submitted for clearing in the United States or because activities related to collateral management of the transaction, such as the exchange of margin, occurred within the United States. See Cross-Border Proposing Release, 78 FR 31000.

167 Non-U.S. persons engaged in security-based swap dealing activity may include persons whose counterparties have legal recourse against a U.S. person arising out of the security-based swap transactions of the non-U.S. person or persons that are conduit affiliates. As noted above, our Cross-Border Adopting Release finalized rules providing that a non-U.S. person must include in its dealer de minimis calculation transactions arising out of its dealing activity with counterparties that are U.S. persons, or such transactions with non-U.S. persons if it is a conduit affiliate or if its counterparty has a right of recourse against a U.S. person under the security-based swap, even if it is not engaging in dealing activity using personnel located in the United States to arrange, negotiate, or execute the transaction. See Exchange Act rules 3a71-3(a)(1), (b)(1)(ii), and (b)(1)(iii)(B). Nothing in the proposed amendment to Exchange Act rule 3a71-3 should be construed to affect any person's obligations created by any of these previously adopted rules.

168 As noted above, some commenters argued that transactions between two non-U.S. persons do not create risk within the United States and should therefore not be subject to Title VII. See note 103, supra. As we have discussed above, however, even if such transactions do not raise counterparty credit risk in the United States, such transactions raise concerns about the integrity and transparency of the U.S. financial market. See discussion in Section III.B.4, supra (citing and responding to comment letters making this argument).

engage in significant relevant dealing activity, including activity engaged in by personnel located in a U.S. branch or office, are required to register as security-based swap dealers and to comply with relevant Title VII requirements applicable to security-based swap dealers.[169]

At the same time, this proposed approach is intended to avoid unnecessary costs and complexity that may make it difficult for market participants to comply with such requirements. We recognize commenters' concerns that our initially proposed approach to "transactions conducted within the United States" potentially could have imposed significant costs on, and presented compliance challenges to, market participants. As some commenters noted, the initially proposed definition of "transaction conducted within the United States" was sufficiently broad that it might have encompassed conduct within the United States by either counterparty to the transaction that could be characterized as "incidental."[170] In addition, market participants may have incurred costs associated with monitoring the location of relevant personnel acting on behalf of their counterparty and/or obtaining relevant representations from their counterparty on a transaction-by-transaction basis, potentially increasing compliance costs significantly.[171] We

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169 We note that some commenters urged us to abandon an activity-based approach entirely because, in their view, the CFTC had not adopted such an approach and, diverging from the CFTC by imposing such an approach on security-based swap transactions would result in significant additional costs for market participants. See note 111, supra. As noted above, however, although the CFTC has not finalized its view on such an approach, the CFTC Staff Advisory provided the CFTC staff view that non-U.S. swap dealers should comply with certain requirements with respect to swap transactions arranged, negotiated, or executed in the United States. See note 21, supra, and accompanying discussion. Although the CFTC Staff Advisory does not appear to address inclusion of swaps arranged, negotiated, or executed in the United States in the dealer de minimis calculations of non-U.S. persons, the test set forth in proposed Exchange Act rule 3a71-3(b)(1)(iii)(C) is similar to the approach suggested by the CFTC Staff Advisory for determining the applicability of certain transaction-level requirements. See Section III.B.3, supra.

170 See note 104, supra (citing comments expressing concern that the initially proposed definition of "transaction conducted within the United States" would capture incidental conduct within the United States).

171 See notes 108-110, supra.

preliminarily believe that our proposed approach of focusing solely on whether the non-U.S. person engaged in dealing activity is using personnel located in the United States to arrange, negotiate, or execute the security-based swap would address these concerns in a more workable manner. Consistent with this focus on the location of activity carried out by the personnel of the dealer or of its agent, the non-U.S. person engaged in dealing activity would not be required to consider the location of its counterparty's operations (or that of the counterparty's agent) in determining whether the transaction should be included in its own de minimis calculation.

In the following subsections, we describe key elements of the proposed amendment to Exchange Act rule 3a71-3(b)(1)(iii), and address comments of particular relevance with respect to each element.

(a) "Arranging, negotiating, or executing" a security-based swap transaction

Proposed rule 3a71-3(b)(1)(iii)(C) would apply only to transactions connected with a non-U.S. person's security-based swap dealing activity that its personnel (or the personnel of an agent) located in the United States arrange, negotiate, or execute. The proposed approach, accordingly, would reach a narrower range of activity than did the initially proposed rules that included the term "transaction conducted within the United States," which would have included any transaction solicited, negotiated, executed, or booked, by either party, within the United States.[172]

Consistent with our explanation for initially proposing the term "transaction conducted within the United States," we intend, for purposes of the proposed rule, "arrange" and

[172] As noted above, the initially proposed rule would have required non-U.S. persons to include in their de minimis calculation any "transaction conducted within the United States" related to their dealing activity. See Cross-Border Proposing Release, 78 FR 30999-00.

"negotiate" to indicate market-facing activity of sales or trading personnel in connection with a particular transaction, including interactions with counterparties or their agents.[173] Also for purposes of the proposed rule, we intend "execute" to refer to the market-facing act that, in connection with a particular transaction, causes the person to become irrevocably bound under the security-based swap under applicable law. "Arranging," "negotiating," and "executing" also include directing other personnel to arrange, negotiate, or execute a particular security-based swap.[174]

We recognize that several commenters expressed concern about the terms used in our proposed definition of "transaction conducted within the United States"[175] and criticized the use of the terms "arrange, negotiate, or execute" in the CFTC Staff Advisory,[176] objecting to those terms both as ambiguous and as not reflective of how swap dealing activity is actually carried out

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173 See Cross-Border Proposing Release, 78 FR 31000 (noting that "dealing activity is normally carried out through interactions with counterparties or potential counterparties that include solicitation, negotiation, execution, or booking of a security-based swap").

Consistent with the approach taken to the final definition of "transaction conducted through a foreign branch" adopted in the Cross-Border Adopting Release, the proposed amendment includes "arrange" instead of "solicit" in recognition of the fact that a dealer, by virtue of being commonly known in the trade as a dealer, may respond to requests by counterparties to enter into dealing transactions, in addition to actively seeking out such counterparties. See Cross-Border Adopting Release, 79 FR 47322 n.381; 15 U.S.C. 78c(a)(71)(A)(iv). Similarly, the proposed amendment omits reference to where a transaction is booked because, in determining whether dealing activity involving two non-U.S.-person counterparties occurs within the United States, we preliminarily believe it is appropriate to focus on the location of the market-facing activity of personnel arranging, negotiating, or executing the security-based swap on behalf of a non-U.S. person in connection with its security-based swap dealing activity, as it is the market-facing activity that raises the types of concerns described above. Cf. note 115, supra. If the transaction is booked in a U.S. person, of course, that U.S. person is a counterparty to the security-based swap and is required to include the security-based swap in its own de minimis calculation if the transaction is in connection with its dealing activity. See Exchange Act rule 3a71-3(b)(1)(i).

174 In other words, sales and trading personnel of a non-U.S. person who are located in the United States cannot simply direct other personnel in carrying out dealing activity that those personnel would otherwise carry out were those personnel not attempting to avoid application of this rule.

175 See note 115, supra.

176 See, e.g., notes 127 and 129, supra.

by market participants, and therefore as unworkable on a trade-by-trade basis.[177] In response, we clarify that under this proposed amendment, we do not intend market participants to look beyond those personnel who are involved in, or directing, market-facing activity in connection with a particular security-based swap. This should enable market participants to identify the location of relevant activity more efficiently than a test that would require market participants to categorize personnel according to their functions. The proposed amendment would require such market participants to focus on whether sales or trading personnel located in the United States engage in this market-facing activity in connection with a particular transaction, not on where these or other personnel perform internal functions (such as the processing of trades or other back-office activities) in connection with that transaction.[178] Accordingly, the involvement of personnel located in a U.S. branch or office in a transaction, where such personnel do not engage in market-facing activities with respect to a specific transaction (such as a person who designs the security-based swap but does not communicate with the counterparty regarding the contract in connection with a specific transaction and does not execute trades in the contract) would not fall within the scope of the proposed amendment.[179] Accordingly, preparing underlying

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[177] See notes 127 and 129, supra. See also notes 107, 112, and 135, supra.

[178] One commenter urged the CFTC to exclude from Title VII requirements any transaction executed electronically. See note 130, supra (citing Barclays Letter to CFTC). However, we do not think that such an exclusion would be appropriate under our proposed approach given its focus on, among other things, the location of personnel executing the transaction on behalf of the non-U.S. person. To the extent that a non-U.S. person is using personnel located in the United States to execute a security-based swap transaction, that transaction raises regulatory concerns that, at sufficient volumes, warrant regulation under Title VII. In particular, we note that electronic execution does not eliminate concerns about abusive or manipulative conduct. See also Section III.C, infra (discussing proposal to make exception for cleared anonymous transactions unavailable for security-based swaps arranged, negotiated, or executed by personnel located in the United States).

[179] See note 104, supra (citing IIB Letter arguing that ministerial or clerical activity in the United States should not trigger application of Title VII). On the other hand, to the extent that personnel located in a U.S. branch or office engages in market-facing activity normally associated with

documentation for the transaction, including negotiation of a master agreement and related documentation, or performing ministerial or clerical tasks in connection with the transaction as opposed to negotiating with the counterparty the specific economic terms of a particular security-based swap transaction, also would not be encompassed by the proposed approach. We preliminarily believe that activities in the United States that do not involve the arrangement or negotiation of the economic terms of a specific transaction are unlikely to raise the types of concerns addressed by the Title VII requirements that we are proposing to apply to such transactions.[180] Consistent with customary Commission practice, we expect that Commission staff will monitor the practices of market participants as they develop under any final rules that we adopt and, if necessary and appropriate, make recommendations to address such developments.

We preliminarily believe that our proposed amendment should considerably mitigate concerns raised by commenters regarding the scope and workability of an activity-based test for

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sales and trading, the location of that personnel would be relevant, even if the personnel are not formally designated as sales persons or traders.

[180] Similarly, a transaction would not be captured under the proposed amendment merely because a U.S.-based attorney is involved in negotiations regarding the terms of the transaction.

We also are not proposing to include either submitting a transaction for clearing in the United States or reporting a transaction to an SDR in the United States as activity that would cause a transaction to be arranged, negotiated, or executed by personnel located in the United States under the proposed rule, nor are we proposing to treat activities related to collateral management (*e.g.*, exchange of margin payments) that may occur in the United States or involve U.S. banks or custodians as activity conducted within the United States for these purposes. We recognize that submission of a transaction for clearing to a CCP located in the United States poses risk to the U.S. financial system, and collateral management plays a vital role in an entity's financial responsibility program and risk management. However, we preliminarily believe that none of these activities, by themselves, would raise the types of concerns associated with dealing activity. See Cross-Border Proposing Release, 78 FR 31000. Cf. note 116, supra (citing comment letter urging that application of Title VII not be triggered by the location at which a transaction is cleared).

application of Title VII requirements.[181] Because the proposed amendment requires a non-U.S. person to include a security-based swap in its de minimis calculation based solely on where it (and not its counterparty) arranges, negotiates, or executes the security-based swap, a non-U.S. person that is acting in a dealing capacity in a particular transaction would need to identify the location of its personnel (or that of its agent's personnel) involved in market-facing activity with respect to the transaction, but not the location of its counterparty.[182]

Some commenters urged that an activity-based test, if implemented, should look only to where the relevant transaction was executed, or where the dealer's personnel committed the dealer to the trade.[183] Although we recognize that focusing solely on where a security-based swap was executed (and not where it was arranged or negotiated) may meaningfully reduce certain costs associated with the proposed amendment, we preliminarily believe that looking solely to the location of execution could permit non-U.S. persons engaged in security-based swap dealing activity using personnel located in a U.S. branch or office to avoid falling within the definition of "security-based swap dealer" simply by ensuring that execution is performed by personnel located outside the United States, even if the non-U.S. person uses personnel located

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181 See, e.g., notes 108-110 and 115, supra.

182 One commenter supported the initially proposed term "transaction conducted within the United States" in part because the commenter believed that it would help capture offshore funds with a "U.S. nexus," given that it would have encompassed all security-based swap trading activity carried out by investment managers within the United States. See note 26, supra (citing Citadel Letter). Under the narrower scope of activity captured in our proposed amendment, such activity of a person not engaged in dealing activity would not require the transaction to be included in the de minimis threshold calculation of its dealer counterparty. We note, however, that our rule defining "principal place of business in the United States" as applied to externally managed investment vehicles should help ensure that those funds whose security-based swap activities may pose risks to U.S. financial institutions, even when transacting with non-U.S. dealers, are treated as U.S. persons. See Exchange Act rule 3a71-3(a)(4)(ii); Cross-Border Adopting Release, 79 FR 47310.

183 See notes 129-130, supra.

in a U.S. branch or office to perform all other key aspects of its dealing activity. We also note that the "security-based swap dealer" definition encompasses a number of activities, including holding oneself out as a dealer or market-making,[184] which suggests that it is appropriate to focus on the location of a wider range of market-facing activity.

(b) "Located in a U.S. branch or office"

Proposed rule 3a71-3(b)(1)(iii)(C) would apply only to transactions connected with a non-U.S. person's security-based swap dealing activity that are arranged, negotiated, or executed by personnel located in a U.S. branch or office.[185] This element of the proposed amendment should mitigate the likelihood, noted by several commenters,[186] that a non-U.S.-person dealer would be required to include in its de minimis calculations transactions that involve activity by personnel of the non-U.S. person or personnel of its agent who are not assigned to a U.S. branch or office, but instead are only incidentally present in the United States when they arrange, negotiate, or execute the transaction. The proposed amendment generally would not require a non-U.S. person to consider activity of personnel who are not located in a U.S. branch or office, such as participation in negotiations of the terms of a security-based swap by an employee of the

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184 See Exchange Act section 3(a)(71)(A)(ii); Intermediary Definitions Adopting Release, 77 FR 30617-18.

185 As noted above, however, if personnel located in a non-U.S. branch or office are arranging, negotiating, or executing a particular security-based swap at the specific direction (i.e., engaging in dealing activity of the U.S. person that the U.S. person would carry out itself were it not attempting to avoid Title VII) of personnel located in a U.S. branch or office, we would view that transaction as having been arranged, negotiated, or executed by the personnel located in the United States. See note 174 and accompanying text, supra.

186 See note 104, supra (citing comments expressing concern that the initially proposed definition of "transaction conducted within the United States" would capture incidental conduct within the United States).

dealer assigned to a foreign office who happens to be traveling within the United States.[187] We preliminarily believe that this type of activity is incidental and therefore not likely to raise the concerns that the proposed approach is intended to address to the same degree as dealing activity carried out by personnel who are located in a U.S. branch or office.[188]

The proposed amendment would, however, not exclude security-based swap transactions that the non-U.S. person, in connection with its dealing activity, arranges, negotiates, or executes, using personnel located in a U.S. branch or office to respond to inquiries from a non-U.S.-person counterparty outside business hours in the counterparty's jurisdiction. We preliminarily believe that a non-U.S. person that uses sales or trading personnel located in a U.S. branch or office to engage in market-facing activity in connection with its dealing activity is likely to raise Title VII concerns, regardless of either counterparty's motivations for entering into the transaction.[189] Accordingly, we preliminarily do not believe that it would be appropriate to exclude from the de minimis calculation transactions arising from such activity by personnel located in a U.S. branch or office because their assignment to a U.S. branch or office suggests that the presence of such personnel in the United States is not "incidental."

We preliminarily believe that this element of the proposed amendment also should mitigate the burdens associated with determining whether a particular transaction needs to be

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187 Because proposed Exchange Act rule 3a71-3(b)(1)(iii)(C) applies only to the security-based swap dealing activity, it does not limit, alter, or address any guidance regarding our views or interpretation of any similar provisions of the federal securities laws, including those applicable to brokers or dealers under the Exchange Act, or investment advisers under the Investment Advisers Act of 1940, Commission rules, regulations, interpretations, or guidance.

188 See Section III.B.4, supra.

189 One commenter described these transactions as being carried out on an "exception basis." See IIB Letter to CFTC at 12. See also note 143, supra. Other commenters urged us not to use "incidental" activity in the United States to trigger application of Title VII or suggested that we establish a materiality threshold. See note 104, supra (citing MFA/AIMA Letter and SIFMA/FIA/FSR Letter).

included in a non-U.S. person's de minimis calculation.[190] We acknowledge that the proposed amendment potentially would lead a market participant to perform a trade-by-trade analysis to determine the location of relevant personnel performing market-facing activity in connection with the transaction. However, because the proposed amendment encompasses a person's dealing activity only when its personnel or personnel of its agent located in a U.S. branch or office have arranged, negotiated, or executed the transaction, a non-U.S. person performing this analysis should be able to identify for purposes of ongoing compliance the specific sales and trading personnel whose involvement in market-facing activity would require a transaction to be included in its de minimis calculation.[191] Alternatively, such non-U.S. person may establish policies and procedures that would facilitate compliance with this proposed amendment by requiring transactions connected with its dealing activity to be arranged, negotiated, and executed by personnel located outside the United States.[192]

(c) "Personnel of such non-U.S. person" or "personnel of an agent"

Proposed rule 3a71-3(b)(1)(iii)(C) would apply to transactions connected with a non-U.S. person's security-based swap dealing activity that are arranged, negotiated, or executed by personnel located in a U.S. branch or office, whether the non-U.S. person arranges, negotiates, or executes the transaction directly using its own personnel located in a U.S. branch or office, or does so using personnel of an agent of such non-U.S. person, located in a U.S. branch or office.

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190 See notes 108-110, and 133-134, supra.

191 We preliminarily believe that persons engaged in dealing activity may already identify personnel involved in market-facing activity with respect to specific transactions in connection with regulatory compliance policies and procedures and to facilitate compensation.

192 In addition, we note that some market participants engaged in both swap dealing and security-based swap dealing activity may perform a similar analysis consistent with CFTC Staff Advisory, which clarifies the CFTC staff's view that Title VII requirements apply to transactions arranged, negotiated, or executed in the United States by, or on behalf of, swap dealers. See notes 21 and 169, supra, and accompanying discussion.

As noted above, a non-U.S. person engaged in security-based swap dealing activity with other non-U.S. persons, if it wishes to avail itself of the expertise of sales, trading, and other personnel located in the United States, may carry out that activity using its own personnel located in a U.S. branch or office, or using the personnel of its agent, located in a U.S. branch or office.[193] We preliminarily believe that dealing activity carried out within the United States by a non-U.S. person is likely to raise the concerns that the proposed approach is intended to address,[194] whether that dealing activity is carried out by the non-U.S. person's personnel located in a U.S. branch or office or on its behalf by the personnel of its agent, located in a U.S. branch

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193 For purposes of proposed rule 3a71-3(b)(1)(iii)(C), we would interpret the term "personnel" in a manner consistent with the definition of "associated person of a security-based swap dealer" contained in section 3(a)(70) of the Exchange Act, 15 U.S.C. 78c(a)(70), regardless of whether such non-U.S. person or such non-U.S. person's agent is itself a security-based swap dealer. This definition is, in turn, substantially similar to the definition of "associated person of a broker or dealer" in section 3(a)(18) of the Exchange Act, 15 U.S.C. 78c(a)(18). The definition in section 3(a)(18) is intended to encompass a broad range of relationships that can be used by firms to engage in and effect securities transactions, and is not dependent solely on whether a natural person is technically an "employee" of the entity in question. See Alexander C. Dill, Broker-Dealer Regulation Under the Securities Exchange Act of 1934: The Case of Independent Contracting, 1994 COLUM. BUS. L. REV. 189, 211-213 (1994) (noting that the Securities Act Amendments of 1964, which amended section 3(a)(18) of the Exchange Act, "rationalized and refined the concept of 'control' by firms over their sales force by introducing the concept of an 'associated person' of a broker-dealer."). Accordingly, we would expect to examine whether a particular entity is able to control or supervise the actions of an individual when determining whether such person is considered to be "personnel" of a U.S. branch, office, or agent of a security-based swap dealer. This is particularly relevant in the context of a financial group that engages in a security-based swap dealing business, where personnel of one affiliate may operate under the direction of, or in some cases, report to personnel of another affiliate within the group. See also Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds, BHCA-1 (Dec. 10, 2013), 59 FR 5535, 5591 (Jan. 31, 2014) (explaining, in the context of adopting certain provisions of what is commonly referred to as the Volcker Rule, that the relevant "trading desk" of a banking entity "may manage a financial exposure that includes positions in different affiliated legal entities" and similarly "may include employees working on behalf of multiple affiliated legal entities or booking trades in multiple affiliated entities") (internal citations omitted).

194 See Section III.B.4, supra.

or office.[195] Accordingly, we are proposing to require non-U.S. persons to include in their de minimis calculations any transactions in connection with their security-based swap dealing activity that are arranged, negotiated, or executed by personnel of such persons located in a U.S. branch or office, or by personnel of its agent located in a U.S. branch or office.[196]

We considered the view of at least one commenter that our existing broker-dealer regime would be sufficient to address any concerns raised by personnel of its agent in the United States acting on behalf of a non-U.S. person engaged in security-based swap dealing activity.[197] Because the Exchange Act defines security-based swaps as securities, an agent acting on behalf of a non-U.S. person that is engaged in security-based swap dealing activity generally would be

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195 We preliminarily believe that it is appropriate for the proposed amendment to take into account where personnel of the non-U.S. person's agent are arranging, negotiating, or executing the transaction on behalf of the non-U.S. person, regardless of whether the agent is affiliated with the non-U.S. person, as security-based swap dealing activity carried out through an unaffiliated agent may raise the same concerns as such activity carried out through an affiliated agent. See note 164, supra.

196 Two commenters raised concerns that our initially proposed rule could put U.S. brokers and investment managers at a competitive disadvantage by subjecting all security-based swap transactions in which they are involved, including those in which they are performing services on behalf of non-U.S. persons, to the relevant provisions of Title VII under the initially proposed definition of "transaction conducted within the United States." See note 113, supra (citing IIB Letter and SIFMA/FIA/FSR Letter); note 104, supra (citing Pensions Europe Letter, IAA Letter, and ICI Letter). The re-proposed approach should mitigate this concern on the part of investment managers, as proposed Exchange Act rule 3a71-3(b)(1)(iii)(C) would look only to the location of the dealing counterparty's activity, meaning that the location of the investment adviser will be immaterial to its dealing counterparty's de minimis calculation under the proposed amendment. This approach would also address concerns expressed by one commenter that private funds may have difficulty identifying whether their dealer counterparties are engaged in dealing activity in the United States. See note 106, supra.

However, under the proposed approach a non-U.S. person that uses a broker as its agent to arrange, negotiate, or execute security-based swap transactions in connection with that non-U.S. person's dealing activity would be required to include those transactions in its own de minimis calculations. We recognize that this approach may make certain brokers less able to compete for the business of non-U.S.-person dealers that would otherwise not be arranging, negotiating, or executing transactions using personnel located in a U.S. branch or office, but given the regulatory concerns such transactions may raise, we think it is appropriate to require such transactions to be included in the non-U.S. person's de minimis threshold calculations. See Section III.B.4, supra.

197 See IIB Letter at 10.

required to register as a broker and, with respect to the transactions that it intermediates, could be required to comply with relevant Exchange Act requirements with respect to those transactions.[198] The commenter suggested that direct regulation of this agent would address "most of the . . . objectives to be served by [security-based swap dealer] registration, as well as the external business conduct standards."[199]

After careful consideration of this alternative approach, we have preliminarily concluded that broker-dealer regulation would not, on its own, adequately address the concerns raised by agents located in the United States acting on behalf of non-U.S. persons to facilitate the security-based swap dealing activity of such non-U.S. persons. Given the range of regulatory concerns such activity raises,[200] we preliminarily believe that, irrespective of any other regulatory framework that may apply to the agent, the non-U.S. person engaged in security-based swap

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198 Title VII of the Dodd-Frank Act amended the Exchange Act definition of "security" to encompass security-based swaps. See Exchange Act section 3(a)(10), 15 U.S.C. 78c(a)(10), as revised by section 761(a)(2) of the Dodd-Frank Act. See also Exchange Act section 3(a)(4) (defining "broker"). We previously granted temporary exemptive relief from compliance with certain provisions of the Exchange Act in connection with this revision of the statutory requirements in order generally to maintain the status quo during the implementation process for the Dodd-Frank Act. See Order Granting Temporary Exemptions under the Securities Exchange Act of 1934 in Connection with the Pending Revisions of the Definition of "Security" to Encompass Security-Based Swaps, Exchange Act Release No. 64795 (Jul. 1, 2011), 76 FR 39927 (Jul. 7, 2011) ("Exchange Act Exemptive Order"). Among other things, this relief granted temporary exemptions specific to security-based swap activities by registered brokers and dealers. See id. at 39-44. In February 2014, we extended the expiration dates (1) for exemptions that are generally not directly related to specific security-based swap rulemakings until the earlier of such time that we issue an order or rule determining whether any continuing exemptive relief is appropriate for security-based swap activities with respect to any of the Exchange Act provisions or until three years following the effective date of that order; and (2) for exemptions that are directly related to specific security-based swap rulemakings, until the compliance date for the relevant security-based swap rulemaking. See Order Extending Temporary Exemptions under the Securities Exchange Act of 1934 in Connection with the Revision of the Definition of "Security" to Encompass Security-Based Swaps, and Request for Comment, Exchange Act Release No. 71485 (February 5, 2014), 79 FR 7731 (February 10, 2014).

199 IIB Letter at 10.

200 See Section III.B.4, supra.

dealing activity through the agent, if it exceeds the de minimis threshold, should also be subject to security-based swap dealer regulation.[201]

First, as that commenter acknowledged, an agent using personnel located in a U.S. branch or office would not be required to register as a broker-dealer if it could avail itself of certain exceptions under the Exchange Act and the rules or regulations thereunder.[202] Given these exceptions, reliance on the broker-dealer regime to address the regulatory concerns raised by security-based swap dealing activity that a non-U.S. person carries out in the United States through an agent could result in significant non-U.S. person security-based swap dealing activity being carried out using an agent that, because, for example, it is a bank, is not in fact subject to the broker-dealer regulatory framework. We preliminarily believe that this result would not be appropriate, particularly given that, in Title VII, Congress established a new, separate regulatory framework for security-based swap dealers that was designed specifically to encompass the security-based swap dealing activities of banks.[203]

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201 Consistent with our views expressed in prior releases, if a financial group used one entity to perform the sales and trading functions of its dealing business and another to book the resulting transactions, we would "view the booking entity, and not the intermediary that acts as an agent on behalf of the booking entity to originate the transaction, as the dealing entity." Cross-Border Proposing Release, 78 FR 30976. See also Intermediary Definitions Adopting Release, 77 FR 30617 n.264 ("A sales force, however, is not a prerequisite to a person being a security-based swap dealer. For example, a person that engages in dealing activity can fall within the dealer definition even if it uses an affiliated entity to market and/or negotiate those security-based swaps connected with its dealing activity (e.g., the person is a booking entity)."). To the extent that the activities performed by the first person involve arrangement, negotiation, or execution of security-based swaps as agent for the booking entity engaged in dealing activity, our proposed amendment would treat the booking entity's transmission of an order and instructions to the agent as part of the dealing activity of the booking entity itself. As already noted, a person engaged in these activities on behalf of the security-based swap dealer may itself be subject to regulation as a broker under the Exchange Act. See note 198, supra.

202 See note 105, supra (citing IIB Letter). For example, Exchange Act section 3(a)(4)(B) excepts banks from the definition of "broker" with respect to certain activity.

203 See Exchange Act section 15F. Notably, the definition of "security-based swap dealer," unlike the definitions of "broker" and "dealer" under the Exchange Act, does not include any exceptions

Second, even absent the bank exception to the definition of "broker," we are not persuaded that broker-dealer regulation of the agent operating in the United States would address the concerns raised by this security-based swap dealing activity. For example, although regulation of the agent acting as a broker would provide the Commission with access to the books and records of the agent relating to a particular transaction, it would not provide us access to the relevant books and records of the non-U.S.-person dealer on whose behalf the agent is acting, which likely would reduce our ability to monitor that non-U.S. person engaging in the dealing activity for compliance with the securities laws, including with the anti-fraud provisions of those laws.[204]

As noted above, access to books and records is the primary tool for oversight of the financial entity and for conducting market surveillance. But the broker's books and records are likely to be insufficient for this purpose, given that foreign dealers may allocate different duties in connection with a particular security-based swap to their own personnel and other functions to their agents, both in and outside the United States. The records of the agents would not be sufficient to document other market-facing activity of the foreign dealer that is not carried out through the agent, but that may be relevant to identifying activity in the United States both within the security-based swap market as well as in markets for related underlying assets, such as corporate bonds, that, in light of the other security-based swap activity of the foreign dealer, may be abusive or manipulative. We would have access to these books and records necessary to identify fraudulent or abusive conduct on the part of the foreign dealer only if the foreign dealer is required to register as a security-based swap dealer. In addition, identifying certain

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for banks or banking activities. See Exchange Act section 3(a)(71) (defining "security-based swap dealer").

[204] See Section III.B.4, supra.

manipulative or abusive market practices may require information about security-based swap transactions of the non-U.S.-person dealer that are not arranged, negotiated, or executed in the United States. To effectively monitor for fraud and manipulation in a market where a significant proportion of transactions are likely to be carried out by (and between) dealers using these types of business structures, we preliminarily believe that the non-U.S.-person dealers that are the counterparties to these transactions should be required to include these transactions in their de minimis calculations. To the extent that they exceed the relevant thresholds, these dealers would be subject to security-based swap dealer regulation, which would enable the Commission to obtain access to the dealer's books and records.

6. Other commenter concerns and alternatives

(a) Potential duplication and comity concerns

Some commenters expressed concern that an activity-based approach to the de minimis exception and other Title VII requirements could lead to regulatory conflicts and overlaps,[205] or that it does not adequately take into account the actions and interests of other regulators.[206] As we noted above, Commission staff has participated in numerous bilateral and multilateral discussions with foreign regulatory authorities addressing the regulation of OTC derivatives, and, through these discussions, we have gathered information about foreign regulatory reform efforts and their impact on and relationship with the U.S. regulatory regime.[207]

We recognize that some non-U.S. persons that may be required to register as security-based swap dealers as a result of proposed Exchange Act rule 3a71-3(b)(1)(iii)(C) may already be subject to regulation similar to our security-based swap dealer regulatory framework in other

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[205] See note 105, supra.

[206] See note 295, infra.

[207] See Section I.B, supra.

jurisdictions. At the same time, we preliminarily believe that it is appropriate to regulate dealing activity that occurs within the United States, including by subjecting to security-based swap dealer registration non-U.S. persons that exceed the relevant de minimis threshold by virtue of security-based swap dealing activity involving the arrangement, negotiation, or execution of security-based swaps on behalf of such person by personnel located in a U.S. branch or office.[208] We previously have proposed to provide the opportunity for substituted compliance with respect to certain security-based swap dealer requirements as set forth in our Cross-Border Proposing Release.[209] We received comments on this proposal, which we continue to consider, and we continue preliminarily to believe that the appropriate means of addressing potential overlap or duplication is through substituted compliance rather than by forgoing regulation entirely.[210]

(b) Reliance on representations

At least one commenter specifically requested that we retain the provision in the proposal permitting reliance on a representation concerning whether a counterparty was engaging in

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[208] As noted above, one commenter specifically argued that the initially proposed approach would subject U.S. branches of EU banks to duplicative regulations because EU regulations also apply to the transactions of such branches. See note 105, supra. We do not believe the possibility that a person may be subject to similar regulation by a foreign regulatory authority can be determinative of the scope of our regulatory framework, given the specific authority Congress provided us to regulate, among other things, security-based swap dealing activity in the United States and given the potential for differences in regulatory interests and in supervisory and enforcement priorities among different regulatory jurisdictions. We also note that EU regulations similarly apply to transactions between two EU branches of U.S. banks. See Commission Delegated Regulation supplementing Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 with regard to regulatory technical standards on direct, substantial and foreseeable effect of contracts within the Union and to prevent the evasion of rules and obligations, Article 2(1).

[209] See Cross-Border Proposing Release, 78 FR 31088-90 (discussing proposed substituted compliance framework for security-based swap dealers); id. at 31024-25 (same).

[210] See Cross-Border Proposing Release, 78 FR 31088-90 (describing proposed substituted compliance framework for foreign security-based swap dealers); initially proposed Exchange Act rule 3a71-5 (providing for substituted compliance with respect to security-based swap dealer requirements).

activity within the United States.[211] The proposed amendment does not incorporate such a provision, as the more limited scope of the re-proposed rule appears to make it unnecessary in this context. The proposed rule would focus solely on the conduct of a non-U.S. person acting in a dealing capacity, and only that person is required to account for such activity in its de minimis calculations. Accordingly, whether one counterparty's dealing activity occurs within or outside the United States has no legal effect on the obligations of the other counterparty under the proposed rule, and the location of the other counterparty has no effect on whether the transaction falls within the scope of the proposed rule.[212]

7. Request for comment

We request comment on all aspects of the discussion and analysis above, including the following:

- Is our understanding of the global nature of the security-based swap market accurate? If not, why not?
- Is our understanding of the dealing structures used by U.S. and non-U.S. persons accurate? If not, why not? Are there other dealing structures used by market participants?
- Is our understanding of the use of affiliated or unaffiliated persons, such as registered broker-dealers in the United States (including inter-dealer brokers) accurate? If not, why not?

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211 See note 117, supra.

212 Also for this reason, the re-proposed approach addresses comments regarding potential difficulties private funds may have in obtaining such representations from their dealer counterparties. See id. (citing MFA/AIMA Letter). See also note 106, supra.

- Should a non-U.S. person that engages in dealing activity with other non-U.S. persons be required to consider, for purposes of counting a transaction towards its de minimis calculation, the location of its counterparty's dealing activity in addition to the location of its own or its agent's dealing activity? Would the proposed amendment requiring such a non-U.S. person to consider only the location of its own dealing activity appropriately mitigate commenters' concerns while also ensuring that a non-U.S. person that engages in significant levels of dealing activity using personnel located in the United States would be subject to regulation as a security-based swap dealer?
- Does proposed rule 3a71-3(b)(1)(iii)(C), which would apply only to transactions connected with a non-U.S. person's security-based swap dealing activity that it (or its agent) arranges, negotiates, or executes using personnel located in a U.S. branch or office, appropriately focus on activity that is likely to raise the types of concern addressed by Title VII? Is it appropriate to generally focus on market-facing activities? Is the scope of activities too narrow or too broad? Why? Will the approach be workable for market participants? Why or why not?
- Is the use of the terms "arrange," "negotiate," and "execute" in the release and rule text sufficiently clear? How could the terms be further clarified if necessary?
- Is the focus on market-facing activities of the sales and trading desks appropriate in identifying transactions between two non-U.S. persons that should be subject to Title VII requirements?
- Does the change to proposed rule 3a71-3(b)(1)(iii)(C) that would require transactions to be included in a person's de minimis calculation only if personnel

arranging, negotiating, or executing the security-based swap are "located in a U.S. branch or office" address the type of activity within the United States that is likely to raise concerns under Title VII? Is the approach too narrow or too broad? Why?

- Should the proposed amendment incorporate an exception from security-based swap dealer regulation for a non-U.S. person that arranges, negotiates, or executes transactions using personnel of its agent located in a U.S. branch or office to the extent that the agent is a registered broker-dealer? If so, how should this dealing activity be regulated? Specifically, to the extent that security-based swap brokering activity is carried out by personnel of the non-U.S. person engaged in dealing activity who are located in a U.S. branch or office, how should we address it? To the extent that security-based swap brokering activity is carried out by a bank, how should we regulate it? How would we obtain access to the books and records for transactions outside the United States of an unregistered dealer also doing business in the United States through a broker to monitor for market manipulation or other abusive practices?
- Do you agree with proposed rule 3a71-3(b)(1)(iii)(C), which requires a non-U.S. person to include in its de minimis calculation, transactions that it arranges, negotiates, or executes using personnel of an affiliated agent of such non-U.S. person located in a U.S. branch or office?
- Do you agree with proposed rule 3a71-3(b)(1)(iii)(C), which requires a non-U.S. person to include in its de minimis calculation, transactions that it arranges,

negotiates, or executes using personnel of an unaffiliated agent of such non-U.S. person located in a U.S. branch or office?

- What types of controls would be necessary to ensure that a non-U.S. person engaged in dealing activity counts transactions that it is required to include in its dealer de minimis calculations under proposed rule 3a71-3(b)(1)(iii)(C)? How would this work as an operational matter?
- Is this proposed approach to applying Title VII to transactions connected with a non-U.S. person's security-based swap dealing activity that it (or its agent) arranges, negotiates, or executed using personnel located in a U.S. office workable in light of the approach set forth in the CFTC Staff Advisory? Why or why not?

C. Availability of the Exception for Cleared Anonymous Transactions

1. Proposed rule

Under Exchange Act rule 3a71-5, a non-U.S. person, other than a conduit affiliate, is not required to include in its de minimis calculation "transactions that are entered into anonymously on an execution facility or national securities exchange and are cleared through a clearing agency."[213] As we noted in the Cross-Border Adopting Release, this rule is intended to avoid putting market participants in a position where they are required to determine the treatment of the transaction under the de minimis exception in circumstances where the information necessary to that determination (e.g., the U.S.-person status of the counterparty) is unavailable to them.[214] We also noted that, absent such an exception, execution facilities outside the United States might

[213] Exchange Act rule 3a71-5.

[214] See Cross-Border Adopting Release, 79 FR 47325 n.412.

determine to exclude U.S. market participants to prevent a non-U.S. market participant from potentially being required to register as a security-based swap dealer based on information unavailable to the non-U.S. market participant at the time of the transaction.[215]

We are proposing to amend rule 3a71-5 by adding new paragraph (c) to make this exception unavailable to transactions that non-U.S. persons would be required to count under proposed Exchange Act rule 3a71-3(b)(1)(iii)(C). We preliminarily believe that excepting such transactions would be inconsistent with the purposes underlying the requirement that a non-U.S. person include transactions arranged, negotiated, or executed by personnel located in a U.S. branch or office in connection with its dealing activity in its de minimis calculations. To the extent that a non-U.S. person is, in connection with its dealing activity, arranging, negotiating, or executing security-based swap transactions using personnel located in a U.S. branch or office, it raises the concerns described above,[216] regardless of whether such transactions are entered into over-the-counter or on an SB SEF or national securities exchange. Requiring a non-U.S. person to include these transactions in its dealer de minimis calculations does not appear to raise the concerns that led us to adopt Exchange Act rule 3a71-5, given that proposed Exchange Act rule 3a71-3(b)(1)(iii)(C) requires the non-U.S. person to look only to the location of its own security-based swap dealing activity in determining whether it is required to count the trade against its de minimis threshold. Finally, as with disparities in the application of Title VII to transactions arranged, negotiated, or executed in the United States more generally,[217] we note that, if a non-U.S. person could avail itself of this exception even when arranging, negotiating, or executing a

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215 See Cross-Border Adopting Release, 79 FR 47325.

216 See Section III.B.4, supra.

217 See Section II.A, supra (discussing competitive effects of disparate regulatory treatment of activity in the United States); notes 114 and 138, supra (citing comment letters expressing concern about potential competitive disparities).

transaction in connection with its dealing activity using personnel located in a U.S. branch or office, it could have a significant competitive advantage over U.S. persons, even with respect to transactions that are executed on an SB SEF or national securities exchange and cleared on a clearing agency located in the United States.

2. Request for comment

We request comment on all aspects of the proposed amendment regarding availability of the exception for cleared, anonymous transactions with respect to identifying security-based swap transactions that do not need to be included in the de minimis threshold calculations of non-U.S. persons, including the following:

- With respect to transactions that a non-U.S. person would be required to count under proposed rule 3a71-3(b)(1)(iii)(C), should there be an exception from counting such transactions if they are entered into anonymously on an SB SEF or national securities exchange and are cleared through a clearing agency? Why or why not?
- Do security-based swap transactions entered into anonymously on an SB SEF or national securities exchange and cleared through a clearing agency mitigate the risk of fraud or market abuse or other concerns with respect to transactions between two non-U.S. persons that are arranged, negotiated, or executed by personnel located in a U.S. branch or office? Why or why not?

IV. Application of the External Business Conduct Requirements to the Foreign Business and U.S. Business of Registered Security-Based Swap Dealers

A. Overview

In the Cross-Border Proposing Release, we proposed an approach to the application of the security-based swap dealer requirements set forth in section 15F of the Exchange Act that

would classify each of these requirements either as entity-level requirements, which apply to the dealing entity as a whole, or as transaction-level requirements, which apply to specific transactions. In this taxonomy, entity-level requirements include requirements relating to capital and margin, risk management procedures, recordkeeping and reporting, supervision, and designation of a chief compliance officer.[218] Transaction-level requirements include, among others, requirements relating to external business conduct and segregation, which are intended primarily to protect counterparties by requiring registered security-based swap dealers to, among other things, provide certain disclosures to counterparties, adhere to certain standards of business conduct, and segregate customer funds, securities, and other assets.[219]

We proposed generally to apply all requirements in section 15F of the Exchange Act, and the rules and regulations thereunder, to both registered U.S. and foreign security-based swap dealers.[220] We also proposed to establish a policy and procedural framework under which we would consider permitting substituted compliance for registered foreign security-based swap dealers under certain circumstances (but not for registered U.S. security-based swap dealers).[221] We proposed, however, to except the foreign business of registered security-based swap dealers from the external business conduct requirements.[222]

We are re-proposing this exception, which, as originally proposed, incorporated the term "transaction conducted within the United States," to reflect the re-proposed approach to identifying relevant security-based swap activity of registered foreign security-based swap

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218 See Cross-Border Proposing Release, 78 FR 31009.

219 See id.

220 See id.

221 See id. at 31088.

222 See id. at 31016.

dealers that they carry out using personnel located in the United States. We continue to believe that the foreign business of registered security-based swap dealers should be excepted from the external business conduct requirements of Title VII. We also preliminarily believe that it is desirable that the types of activities in the United States that trigger application of the external business conduct requirements to transactions of a registered foreign security-based swap dealer with another non-U.S. person should be identical to those that require a transaction to be included in a non-U.S. person's de minimis threshold calculations, as a consistent test should be more workable for market participants to implement and we preliminarily believe that the proposed test captures the activity that is likely to raise concerns about business conduct in the United States. Accordingly, we are re-proposing initially proposed Exchange Act rule 3a71-3(c) and related definitions solely to conform to the proposed amendments to the de minimis exception.[223]

B. Statutory Framework for External Business Conduct

Section 15F(h) of the Exchange Act requires the Commission to adopt rules specifying external business conduct standards for registered security-based swap dealers in their dealings with counterparties,[224] including counterparties that are "special entities."[225] Congress granted

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223 This proposal does not address application of any of the other elements of the Title VII security-based swap dealer requirements described in the Cross-Border Proposing Release, including those related to the application of entity-level requirements to security-based swap dealers; the application of segregation requirements under Exchange Act section 3E, and the rules and regulations thereunder; and the availability of the opportunity for substituted compliance (including initially proposed Exchange Act rule 3a71-5, which set forth, among other things, the process for submitting substituted compliance determination requests and the standard we would use in evaluating those requests). We anticipate addressing the comments on these elements of that proposal in the context of our consideration of final rules regarding each of the respective security-based swap dealer requirements.

224 Exchange Act section 15F(h)(6), 15 U.S.C. 78o-10(h)(6), directs the Commission to prescribe rules governing external business conduct standards for security-based swap dealers.

the Commission broad authority to promulgate business conduct standards that the Commission determines to be appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Exchange Act.[226]

These standards, as described in section 15F(h)(3) of the Exchange Act, must require security-based swap dealers to: (i) verify that a counterparty meets the eligibility standards for an eligible contract participant; (ii) disclose to the counterparty material information about the security-based swap, including material risks and characteristics of the security-based swap, and material incentives and conflicts of interest of the security-based swap dealer in connection with the security-based swap; and (iii) provide the counterparty with information concerning the daily mark for the security-based swap. Section 15F(h)(3) also directs the Commission to establish a duty for security-based swap dealers to communicate information in a fair and balanced manner based on principles of fair dealing and good faith and to establish other standards as the Commission determines are in furtherance of the purposes of the Exchange Act.

In addition, section 15F(h)(4) of the Exchange Act requires that a security-based swap dealer that "acts as an advisor to a special entity" must act in the "best interests" of the special entity and undertake "reasonable efforts to obtain such information as is necessary to make a reasonable determination" that a recommended security-based swap is in the best interests of the

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225 Exchange Act section 15F(h)(2)(C), 15 U.S.C. 78o-10(h)(2)(C) (defining "special entities"). As discussed below, we have previously proposed business conduct rules and continue to consider comments received on that proposal. See IV.C.1, infra. We intend to address these comments in a subsequent adopting release finalizing rules establishing external business conduct standards, including provisions applicable in transactions with "special entities."

226 See Exchange Act section 15F(h)(3)(D), 15 U.S.C. 78o-10(h)(3)(D) ("[b]usiness conduct requirements adopted by the Commission shall establish such other standards and requirements as the Commission may determine are appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this Act"). See also Exchange Act section 15F(h)(1)(D) (requiring security-based swap dealers to comply with "such business conduct standards . . . as may be prescribed by the Commission by rule or regulation that relate to . . . such other matters as the Commission determines to be appropriate").

special entity.[227] Section 15F(h)(5) requires that a security-based swap dealer that enters into, or offers to enter into, security-based swaps with a special entity comply with any duty established by the Commission that requires the security-based swap dealer to have a "reasonable basis" for believing that the special entity has an "independent representative" that meets certain criteria and undertakes a duty to act in the "best interests" of the special entity.

C. Prior Proposals

1. Business Conduct Proposal

We have proposed rules 15Fh-1 through 15Fh-6 under the Exchange Act to implement the business conduct requirements described above.[228] In addition to external business conduct standards expressly addressed by Title VII, we have proposed certain other business conduct requirements for security-based swap dealers that we preliminarily believed would further the principles that underlie the Dodd-Frank Act. These rules would, among other things, impose certain "know your counterparty" and suitability obligations on security-based swap dealers, as well as restrict security-based swap dealers from engaging in certain "pay to play" activities and provide certain protections for "special entities."[229]

2. Cross-Border Proposing Release

In the Cross-Border Proposing Release, we proposed a rule that would have provided that a registered foreign security-based swap dealer and a foreign branch of a registered U.S. security-based swap dealer, with respect to their foreign business, shall not be subject to the

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227 See Business Conduct Standards for Security-Based Swap Dealers and Major Security-Based Swap Participants ("Business Conduct Proposal"), Exchange Act Release No. 64766 (June 29, 2011), 76 FR 42423-25 (July 18, 2011).

228 See Business Conduct Proposal, 76 FR 42396.

229 See Business Conduct Proposal, 76 FR 42399-400; proposed Exchange Act rules 15Fh-3(e) ("know your counterparty"), 15Fh-3(f) ("suitability"), and 15Fh-6 ("pay to play").

requirements relating to external business conduct standards described in section 15F(h) of the Exchange Act,[230] and the rules and regulations thereunder, other than the rules and regulations prescribed by the Commission pursuant to section 15F(h)(1)(B).[231]

As described more fully in the Cross-Border Proposing Release, the proposed rule would have defined "U.S. business" and "foreign business" with respect to both foreign and U.S. security-based swap dealers. For a foreign security-based swap dealer, "U.S. business" would have been defined to mean (i) any transaction entered into, or offered to be entered into, by or on behalf of such foreign security-based swap dealer, with a U.S. person (other than with a foreign branch), or (ii) any transaction conducted within the United States.[232] For a U.S. security-based swap dealer, "U.S. business" would have been defined to mean any transaction by or on behalf of such U.S. security-based swap dealer, wherever entered into or offered to be entered into, other than a transaction conducted through a foreign branch with a non-U.S. person or another

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230 15 U.S.C. 78o-10(h).

231 See Cross-Border Proposing Release, 78 FR 31016. Section 15F(h)(1)(B) requires registered security-based swap dealers to conform with such business conduct standards relating to diligent supervision as the Commission shall prescribe. See 15 U.S.C. 78o-10(h)(1)(B). All other requirements in section 15F of the Exchange Act, and the rules and regulations thereunder, would apply to both U.S. and registered foreign security-based swap dealers, although we proposed to establish a framework under which we would consider permitting substituted compliance for foreign security-based swap dealers under certain circumstances (but not for U.S. security-based swap dealers, even when they conduct dealing activity through foreign branches). See id. The approach under the initially proposed rule would not have affected applicability of the general antifraud provisions of the federal securities laws to the activity of a foreign security-based swap dealer. See Cross-Border Proposing Release, 78 FR 31016 n.476.

232 See id. at 31016. Whether the activity in a transaction involving a registered foreign security-based swap dealer occurred within the United States or with a U.S. person for purposes of identifying whether security-based swap transactions are part of U.S. business would have turned on the same factors used in that proposal to determine whether a foreign security-based swap dealer is engaging in dealing activity within the United States or with U.S. persons and whether a U.S. person was conducting a transaction through a foreign branch, as set forth in that proposal. See id.

foreign branch of a U.S. person.[233] With respect to both a foreign security-based swap dealer and a U.S. security-based swap dealer, "foreign business" would have been defined to mean any security-based swap transactions entered into, or offered to be entered into, by or on behalf of the foreign security-based swap dealer or the U.S. security-based swap dealer that do not include its U.S. business.[234]

D. Comments

We received relatively few comments specifically addressing our initially proposed approach to application of the external business conduct requirements to security-based swap dealers. One commenter disagreed with our proposed approach with respect to U.S. security-based swap dealers, arguing that all transactions of such persons must always be subject to external business conduct standards, including those conducted through their foreign branches with non-U.S. persons and foreign branches of U.S. banks.[235]

Two commenters generally agreed with the initially proposed approach but suggested certain modifications to address specific concerns. One commenter generally agreed with the proposed approach that would not have imposed external business conduct requirements with respect to the "foreign business" of a foreign security-based swap dealer but argued that these requirements also should not apply to transactions with non-U.S. regulated funds whose security-based swap activity is managed by a U.S. asset manager.[236] This commenter argued that such funds would not expect to receive the protections of Title VII's business conduct standards merely because they use a U.S. asset manager and expressed concern that such requirements

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233 See id.

234 See id.

235 See Letter from Better Markets to SEC, dated August 21, 2013 ("Better Markets Letter") at 28.

236 See ICI Letter at 11.

would disadvantage these entities because foreign security-based swap dealers might prefer to transact with non-U.S. funds managed by non-U.S. asset managers to avoid compliance with the requirements.[237]

Another commenter argued that the definition of "U.S. business" should be limited to transactions with counterparties that are U.S. persons, and that this definition should apply to the business of U.S. and foreign security-based swap dealers.[238] This commenter argued that adopting a uniform definition of "U.S. business" and eliminating "transaction conducted within the United States" from that definition would better accord with the purpose of the requirements, with counterparty expectations, and with international comity concerns.[239] This commenter further stated that there was insufficient "jurisdictional nexus" to warrant applying the external business conduct requirements to all transactions conducted within the United States, regardless of the U.S.-person status of the counterparties.[240]

E. Discussion

We are re-proposing Exchange Act rule 3a71-3(c) regarding application of the external business conduct requirements, and proposing amendments to Exchange Act rule 3a71-3(a) to define certain terms to conform to the proposed amendments to Exchange Act rule 3a71-3(b)(1)(iii)(C), which identifies relevant security-based swap activity of registered foreign security-based swap dealers in which they engage using personnel located in the United States

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237 See id. This commenter suggested that we modify the proposed definition of "U.S. business" for foreign security-based swap dealers by removing prong (ii) of the initially proposed rule, which includes "any transactions conducted within the U.S." in the definition of "U.S. business." In this commenter's view, this change would help ensure that the transactions of such funds with registered foreign security-based swap dealers are not subject to the external business conduct requirements. See ICI Letter at 11 n.28 and accompanying text.

238 See SIFMA/FIA/FSR Letter at A-24.

239 See id. at A-24 to A-25.

240 See id. at A-25.

for purposes of the de minimis exception. Our general approach, however, remains unchanged: The re-proposed rule would distinguish between "U.S. business" and "foreign business" and except the foreign business of a registered foreign security-based swap dealer and a registered U.S. security-based swap dealer from the external business conduct standards in section 15F(h) and the rules and regulations thereunder (other than rules and requirements prescribed by the Commission pursuant to section 15F(h)(1)(B)) of the Exchange Act, and proposed amendments to Exchange Act rule 3a71-3(a) would incorporate these defined terms in the rule.[241]

Specifically, our re-proposed amendment to Exchange Act rule 3a71-3(a) would modify the initially proposed definition of "U.S. business" with respect to foreign security-based swap dealers to refer to any security-based swap transaction arranged, negotiated, or executed by personnel of the foreign security-based swap dealer located in a U.S. branch or office, or by personnel of its agent located in a U.S. branch or office.[242] The definition of "U.S. business" for

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[241] See proposed Exchange Act rules 3a71-3(a)(6), (7), (8), and (9) (defining, respectively, "U.S. security-based swap dealer," "foreign security-based swap dealer," "U.S. business," and "foreign business"); re-proposed Exchange Act rule 3a71-3(c) (setting forth exceptions from certain external business conduct requirements with respect to the "foreign business" of registered foreign security-based swap dealers and registered U.S. security-based swap dealers).

This proposed approach to external business conduct standards would not except registered security-based swap dealers from the rules and requirements prescribed by the Commission pursuant to section 15F(h)(1)(B) of the Exchange Act with respect to their foreign business. As already noted, section 15F(h)(1)(B) requires registered security-based swap dealers to conform with such business conduct standards relating to diligent supervision as the Commission shall prescribe. See 15 U.S.C. 78o-10(h)(1)(B). We preliminarily believe that it is not appropriate to except registered security-based swap dealers from compliance with such requirements. Because registered security-based swap dealers would be subject to a number of obligations under the federal securities laws with respect to their security-based swap business, we preliminarily believe that having systems in place reasonably designed to ensure diligent supervision would be an important aspect of their compliance with the federal securities laws. Under our Cross-Border Proposing Release, these entity-level requirements would apply to a security-based swap dealer on a firm-wide basis to address risks to the security-based swap dealer as a whole. See Cross-Border Proposing Release, 78 FR 31011.

[242] Proposed Exchange Act rule 3a71-3(a)(8)(i)(B). We intend the proposed rule to indicate the same type of activity by personnel located in the United States as described in Section III.B.5,

foreign security-based swap dealers and U.S. security-based swap dealers would continue to exclude certain transactions involving the foreign branches of U.S. persons.[243] The definitions of "U.S. security-based swap dealer,"[244] "foreign security-based swap dealer,"[245] and "foreign business"[246] would remain unchanged from the initial proposal, as would the text of re-proposed rule 3a71-3(c), which would create the exception to the external business conduct requirements (other than rules and requirements prescribed by the Commission pursuant to section 15F(h)(1)(B)) for the foreign business of registered security-based swap dealers.

We continue to believe that a registered security-based swap dealer should be required to comply with the external business conduct requirements with respect to its U.S. business. The proposed external business conduct standards are intended to bring professional standards of

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supra. Moreover, for purposes of proposed Exchange Act rule 3a71-3(a)(8)(i)(B), we would interpret the term "personnel" in a manner consistent with the definition of "associated person of a security-based swap dealer" contained in section 3(a)(70) of the Exchange Act, 15 U.S.C. 78c(a)(70), regardless of whether such non-U.S. person or such non-U.S. person's agent is itself a security-based swap dealer. See note 193, supra (discussing the Commission's proposed interpretation of the term "personnel" for purposes of proposed rule 3a71-3(b)(1)(iii)(C)).

243 Initially proposed Exchange Act rule 3a71-3(a)(6)(i)(A) provided that the U.S. business of a foreign security-based swap dealer included any transaction with a U.S. person, "other than with a foreign branch." The proposed amendment replaces this language with "other than a transaction conducted through a foreign branch of that person." Similarly, initially proposed Exchange Act rule 3a71-3(a)(6)(ii) provided that the U.S. business of a U.S. security-based swap dealer included any transaction of such dealer, other than transactions conducted through a foreign branch with a non-U.S. person "or another foreign branch." Proposed Exchange Act rule 3a71-3(a)(8)(ii) replaces this language with "or a transaction with a U.S. person counterparty that constitutes a transaction conducted through a foreign branch of the counterparty."

These changes are intended to clarify that the counterparty's activity in each such transaction must meet the definition of "transaction conducted through a foreign branch" set forth in Exchange Act rule 3a71-3(a)(3). These proposed changes are consistent with Exchange Act rule 3a71-3(b)(1)(iii)(A), which permits non-U.S. persons to exclude from the de minimis calculation transactions with U.S. persons, to the extent that such U.S. persons are engaging in transactions conducted through a foreign branch.

244 See proposed Exchange Act rule 3a71-3(a)(6).

245 See proposed Exchange Act rule 3a71-3(a)(7).

246 See proposed Exchange Act rule 3a71-3(a)(9).

conduct to, and increase transparency in, the security-based swap market and to require registered security-based swap dealers to treat parties to these transactions fairly. As noted above, the proposed rules would require, among other things, that registered security-based swap dealers communicate in a fair and balanced manner with potential counterparties and that they disclose conflicts of interest and material incentives to potential counterparties. Imposing these requirements on the U.S. business of registered security-based swap dealers should help protect the integrity of U.S. financial markets for all market participants.

We recognize that, depending on the particular structure used by a registered foreign security-based swap dealer to do business in the United States, its personnel (or personnel of its agent acting on its behalf) in the United States may be subject to other business conduct requirements under U.S. law (such as broker-dealer regulation) that govern the professional interactions of such personnel or agents with counterparties to a security-based swap.[247] We also recognize that these other requirements may afford security-based swap counterparties protections that may appear to be similar in many respects to the Title VII external business conduct standards. We preliminarily believe, however, that, notwithstanding any requirements that may apply to such intermediaries, it is appropriate to impose these Title VII requirements directly on registered foreign security-based swap dealers when they use personnel located in the

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[247] See note 198, supra (discussing the Exchange Act Exemptive Order). The Financial Industry Regulatory Authority ("FINRA") also adopted a rule, FINRA Rule 0180 (Application of Rules to Security-Based Swaps), which temporary limits the application of certain FINRA rules with respect to security-based swaps. On January 14, 2015, FINRA filed a proposed rule change, which was effective upon receipt by the Commission, extending the expiration date of FINRA Rule 0180 to February 11, 2016. See Self-Regulatory Organizations; Financial Industry Regulatory Authority, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Extend the Expiration Date of FINRA Rule 0180 (Application of Rules to Security-Based Swaps), Exchange Act Release No. 74049 (Jan. 14, 2015).

United States to arrange, negotiate, or execute security-based swaps, even with counterparties that are also non-U.S. persons.

We note that, in Title VII, Congress has established a comprehensive framework of business conduct standards that applies to registered security-based swap dealers, and we preliminarily believe that this framework should govern their transactions with counterparties when such transactions raise transparency and market integrity concerns that are addressed by these requirements. Although other business conduct frameworks (such as broker-dealer regulation) may achieve similar regulatory goals, the availability of exceptions may mean that alternative frameworks may not apply to certain business structures used by registered security-based swap dealers to carry out their business in the United States.[248] In our preliminary view, it is appropriate to subject all registered security-based swap dealers engaged in U.S. business to the same external business conduct framework, rather than encouraging a patchwork of business conduct protections under U.S. law that may offer counterparties varying levels of protection with respect to their transactions with different registered security-based swap dealers depending on the business model (or models) that each registered security-based swap dealer has chosen to use in its U.S. business.[249]

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[248] See note 202, supra (noting exception from broker-dealer definition for banks).

[249] Consistent with the view we expressed in the Cross-Border Proposing Release, to the extent that a registered foreign security-based swap dealer uses personnel of an agent to arrange, negotiate, or execute security-based swap transactions from a U.S. branch or office, the dealer and its agent may choose to allocate between themselves specific responsibilities in connection with these external business conduct requirements. See Cross-Border Proposing Release, 78 FR 31026-27. However, we note that the registered foreign security-based swap dealer would remain responsible for ensuring that all relevant Title VII requirements applicable to a given security-based swap transaction are fulfilled. See id. at 31026. As noted above, the agent may also be required to register as a broker (or, potentially, as a security-based swap dealer), or as another regulated entity, depending on the nature of its security-based swap or other activity. See note 198 and accompanying text, supra; Cross-Border Proposing Release, 78 FR 31027 n.574. An agent may, accordingly, be subject to independent business conduct or other requirements with

We also note that imposing these external business conduct requirements on a registered foreign security-based swap dealer when it uses personnel located in a U.S. branch or office to arrange, negotiate, or execute security-based swaps with another non-U.S. person should mitigate competitive disparities between different categories of security-based swap dealers operating in the United States.[250] This concern is particularly acute given the ease with which U.S. security-based swap dealers may seek to avoid such competitive disparities by booking in non-U.S.-person affiliates any transactions arranged, negotiated, or executed by personnel located in the United States. As noted above, this restructuring would allow these dealers to continue using U.S. sales and trading personnel to carry on their security-based swap dealing business in a manner largely unchanged from what we understand to be current business practices while avoiding the external business conduct requirements of Title VII.[251]

We have considered the views of the commenters that opposed imposing external business conduct requirements on transactions between a registered foreign security-based swap dealer and a non-U.S.-person counterparty,[252] but we do not believe that the issues raised by commenters warrant refraining from imposing these requirements on all such transactions. The re-proposed approach, which focuses on a transaction of a registered foreign security-based swap dealer with another non-U.S. person only when the registered foreign security-based swap dealer is using personnel located in the United States to arrange, negotiate, or execute the security-based swap, should mitigate the concerns raised by one commenter regarding the potential effect

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respect to its interactions with the registered foreign security-based swap dealer's counterparties that occur in the course of its intermediation of such transactions.

250 See Section II.A, supra (discussing competitive effects of disparate regulatory treatment of activity in the United States).

251 See Section III.B.4, supra.

252 See, e.g., ICI Letter at 11.

of the initially proposed rule on U.S. fund managers that manage offshore funds, because, to the extent an offshore fund is not a U.S. person by virtue of having its principal place of business in the United States, only the location of personnel of the registered foreign security-based swap dealer or the location of personnel of its agent, and not that of persons acting on behalf of a non-U.S.-person fund in the transaction, would be relevant to whether the transaction is U.S. business or foreign business of the registered foreign security-based swap dealer.[253]

We also disagree with the commenter that suggested that such transactions have an insufficient nexus to the United States to warrant application of the external business conduct requirements and that the external business conduct requirement should apply only to transactions with U.S.-person counterparties.[254] As we discussed in the context of the de minimis exception above, a foreign security-based swap dealer arranging, negotiating, or executing a security-based swap transaction using personnel located in a U.S. branch or office is not solely "transacting a business in security-based swaps without the jurisdiction of the United States."[255] If the Commission adopts a rule that makes substituted compliance available for

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253 See notes 236-237, supra. To the extent that a non-U.S. regulated fund is a U.S. person (including because it has its principal place of business in the United States), a foreign security-based swap dealer would be required to comply with external business conduct requirements in any transaction with that fund because the counterparty is a U.S. person. See proposed Exchange Act rule 3a71-3(a)(8). Cf. Exchange Act rule 3a71-3(b)(1)(iii)(A) (requiring non-U.S. persons to include in their de minimis threshold calculations security-based swap transactions with U.S. persons in connection with their dealing activity); Cross-Border Adopting Release, 79 FR 47320 (describing Exchange Act rule 3a71-3(b)(1)(iii)(A)).

254 See notes 238-240, supra.

255 Exchange Act section 30(c). See also Section III.B.4(b), supra.

As noted above, we do not believe that our proposed approach applies Title VII to persons that are "transact[ing] a business in security-based swaps without the jurisdiction of the United States," within the meaning of section 30(c) of the Exchange Act. An approach that did not treat security-based swaps that a registered foreign security-based swap dealer has arranged, negotiated, or executed using its personnel or personnel of its agent located in the United States as the "U.S. business" of that dealer for purposes of proposed Exchange Act rule 3a71-3(c) would, in our view, reflect an understanding of what it means to conduct a security-based swaps

external business conduct requirements and, pursuant to further Commission action, makes a substituted compliance determination, substituted compliance may be permitted in such transactions.[256]

Our re-proposed rule maintains our initially proposed approach to the foreign business of registered U.S. security-based swap dealers. We recognize that at least one commenter suggested that all transactions of a registered U.S. security-based swap dealer should be subject to the external business conduct requirements of Exchange Act section 15F,[257] but we continue to believe it is appropriate to provide this exception for the foreign business of such persons. As we noted in our initial proposal, the Dodd-Frank Act generally is concerned with the protection of U.S. markets and participants in those markets.[258] We continue to believe that subjecting U.S. security-based swap dealers to the Title VII customer protection requirements with respect to their security-based swap transactions conducted through their foreign branches outside the

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business within the jurisdiction of the United States that is divorced both from Title VII's statutory objectives and from the various structures that non-U.S. persons use to engage in security-based swap dealing activity. But in any event we also preliminarily believe that this proposed rule is necessary or appropriate as a prophylactic measure to help prevent the evasion of the provisions of the Exchange Act that were added by the Dodd-Frank Act, and thus help prevent the relevant purposes of the Dodd-Frank Act from being undermined. See Cross-Border Adopting Release, 79 FR 47291-92 (interpreting anti-evasion provisions of Exchange Act section 30(c)). Without this rule, non-U.S. persons could simply carry on a dealing business within the United States with non-U.S. persons. Permitting this activity could allow these firms to retain full access to the benefits of operating in the United States while avoiding compliance with external business conduct requirements, which could increase the risk of misconduct. See Section III.B.4, supra.

256 As noted above, in the Cross-Border Proposing Release, we proposed an approach to substituted compliance with respect to the external business conduct requirements. See note 223, supra. We received comments on this proposed rule that we continue to consider, and we anticipate addressing those comments in the context of our consideration of final rules regarding the external business conduct requirement.

257 See note 235, supra.

258 See Cross-Border Proposing Release, 78 FR 31018.

United States with non-U.S. persons would not appreciably further the goal of protecting the U.S. market or U.S. market participants.

F. Request for comment

We request comment on all aspects of the re-proposed rule regarding application of the external business conduct requirements to registered security-based swap dealers, including the following:

- The re-proposed rule would apply the external business conduct standards to transactions that a registered foreign security-based swap dealer arranges, negotiates, or executes using personnel located in a U.S. branch or office, even if the counterparty is also a non-U.S. person. Are the external business conduct rules appropriately applied in this release? Should the external business conduct rules be expanded to cover other transactions discussed in this release? Should some or all of the external business conduct standards not apply to these activities? Why or why not? Please be specific in identifying why the concerns addressed by the external business conduct requirements do not arise in this context.
- The re-proposed rule would not apply the external business conduct standards to the foreign business of any registered security-based swap dealer. Should some or all of the external business conduct standards apply to the foreign business of these registered entities? Why or why not? Please be specific as to what policy objectives would be advanced by subjecting transactions resulting from the foreign business of a registered security-based swap dealer to the external business conduct requirement.

- The re-proposed rule would not apply the external business conduct standards to a transaction of a registered U.S. security-based swap dealer that is a transaction conducted through a foreign branch (assuming that the counterparty is a non-U.S. person or is a U.S. person for whom the transaction is also a transaction conducted through a foreign branch). Should some or all of the external business conduct standards apply to these transactions? Why or why not?
- What types of controls would be necessary to identify foreign business and U.S. business and ensure that the registered security-based swap dealer complies with the external business conduct standards with respect to its U.S. business? How would this work as an operational matter? Should U.S. business be generally defined with reference to the type of activity that, if performed in a dealing capacity, triggers the registration requirement?
- Should some or all of the external business conduct rules apply in transactions between a registered foreign security-based swap dealer and a foreign branch of a U.S. bank? Why or why not?
- Should some or all of the external business conduct rules apply in transactions between a registered non-U.S. security-based swap dealer and a non-U.S. person whose obligations under a security-based swap are guaranteed by a U.S. person that is conducted outside the United States? Why or why not?
- What would be the market impact of the re-proposed approach to application of the customer protection requirements? Would non-U.S. persons that engage in dealing activities seek to relocate to locations outside the United States personnel who currently arrange, negotiate, and execute transactions from locations within

the United States? Would the potential benefits of applying external business conduct requirements to transactions that are arranged, negotiated, or executed by a registered foreign security-based swap dealer in the United States reduce any incentives to relocate to locations outside the United States? What are the costs of such relocation? What factors would weigh against relocation in spite of those costs?

- How would the proposed application of the requirements affect the competitiveness of U.S. entities in the global marketplace (both in the United States as well as in foreign jurisdictions)? Would the proposed approach place any market participants at a competitive disadvantage or advantage? Why or why not? What other measures should we consider to implement the transaction-level requirements?

V. Application of Other Requirements to Cross-Border Security-Based Swap Activity

A. Overview

In light of our proposed amendment to Exchange Act rule 3a71-3(b), which would apply the de minimis exception to transactions of a non-U.S. person that are arranged, negotiated, or executed by personnel located in a U.S. branch or office in connection with the non-U.S. person's dealing activity, we have determined also to propose certain amendments to Regulation SBSR to address the applicability of the regulatory reporting and public dissemination requirements to such transactions.[259] However, we are not proposing to subject transactions between two non-U.S. persons that are arranged, negotiated, or executed in the United States to

[259] We also are soliciting comment on whether certain transactions of non-U.S. persons whose obligations under a security-based swap are guaranteed by a U.S. person should be exempt from the public dissemination requirement. See Section V.E.3, infra.

mandatory clearing or trade execution.

B. Previously Proposed and Adopted Rules Relating to Application of Clearing, Trade Execution, Regulatory Reporting, and Public Dissemination Requirements

1. Mandatory clearing and trade execution

In the Cross-Border Proposing Release, we proposed to impose both mandatory clearing and trade execution on "transactions conducted within the United States," subject to certain exceptions. Proposed rules 3Ca-3 and 3Ch-1 would have subjected such transactions to mandatory clearing (provided that we had issued a mandatory clearing determination with respect to the security-based swap) and mandatory trade execution (provided that the transaction had been made available to trade) if a person engaged in a security-based swap transaction that is a "transaction conducted within the United States," as defined in initially proposed Exchange Act rule 3a71-3(a)(5).[260] We also proposed an exception to this general requirement, under which a "transaction conducted within the United States" would not have been subject to the clearing or trade execution requirements if (i) neither counterparty to the transaction was a U.S. person; (ii) neither counterparty's performance under the security-based swap was guaranteed by a U.S. person; and (iii) neither counterparty to the transaction was a foreign security-based swap dealer. We proposed that the clearing and trade execution requirements would not apply to transactions that did not involve any of these three types of counterparties due to our preliminary view that, although such transactions conducted within the United States may give rise to operational risks

[260] In addition, the proposed rules generally would have imposed these requirements on a security-based swap transaction if a counterparty to the transaction is a U.S. person or a non-U.S. person whose counterparty has a right of recourse against a U.S. person. See Cross-Border Proposing Release, 78 FR 31078, 31083. We also proposed an approach to substituted compliance with respect to each requirement. See id. at 31098, 31099-100. Although these provisions of the initial proposal are outside the scope of this release, we received comments on these provisions of the proposed rules, which we continue to consider and anticipate addressing in the context of our consideration of final rules regarding each requirement.

in the United States, the financial risk of such transactions would reside outside the United States.[261]

2. Regulatory reporting and public dissemination

In the Cross-Border Proposing Release, we re-proposed the entirety of Regulation SBSR, including rule 908(a) thereof, which, among other things, would have specified when a security-based swap was subject to the regulatory reporting and public dissemination requirements of Regulation SBSR.[262] Security-based swaps that fell within the proposed definition of "transaction conducted within the United States" would have been among the security-based swaps subjected both to regulatory reporting and to public dissemination under rule 908(a), as re-proposed in the Cross-Border Proposing Release.[263]

We recently adopted rule 908(a)(1), which requires regulatory reporting and public dissemination of security-based swap transactions that (i) have a direct or indirect counterparty[264]

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261 See Cross-Border Proposing Release, 78 FR 31080, 31084.

262 Rule 908(a), as initially proposed, would have required regulatory reporting of any security-based swap that is "executed in the United States or through any means of interstate commerce." See Regulation SBSR Proposing Release, 75 FR 75287. When we re-proposed rule 908(a)(1)(i) in the Cross-Border Proposing Release, we expressed concern that the language in the Regulation SBSR Proposing Release could have unduly required a security-based swap to be reported if it had only the slightest connection with the United States. See Cross-Border Proposing Release, 78 FR 31061.

263 Rule 900(ii), as re-proposed in the Cross-Border Proposing Release, would have defined "transaction conducted within the United States" to have the meaning as given in the definition of the term under previously proposed Exchange Act rule 3a71-3(a)(5)(i).

264 Rule 900(hh) of Regulation SBSR defines "side" to mean "a direct counterparty and any guarantor of that direct counterparty's performance who meets the definition of indirect counterparty in connection with the security-based swap." Rule 900(p) of Regulation SBSR defines "indirect counterparty" to mean "a guarantor of a direct counterparty's performance of any obligation under a security-based swap such that the direct counterparty on the other side can exercise a right of recourse against the indirect counterparty in connection with the security-based swap; for these purposes a direct counterparty has a right of recourse against a guarantor on the other side if the direct counterparty has a conditional or unconditional legally enforceable right, in whole or in part, to receive payments from, or otherwise collect from, the guarantor in connection

that is a U.S. person on either or both sides of the transaction, or (ii) are accepted for clearing by a clearing agency having its principal place of business in the United States. In addition, rule 908(a)(2), as adopted, requires regulatory reporting but not public dissemination of transactions that have a direct or indirect counterparty that is a registered security-based swap dealer or registered major security-based swap participant on either or both sides of the transaction but do not otherwise fall within rule 908(a)(1).[265] We did not, however, include in that final rule a provision addressing a security-based swap transaction that is a "transaction conducted within the United States," noting that commenters had expressed divergent views on this particular element of the re-proposed rule. We also noted that we anticipated seeking additional public comment on whether and, if so, how regulatory reporting and public dissemination requirements should be applied to transactions involving non-U.S. persons when they carry out relevant activities in the United States.[266]

We also previously proposed rule 908(b), which would have provided that, notwithstanding any other provision of Regulation SBSR, a person would not incur any obligation under Regulation SBSR unless the person is:

(1) a U.S. person;

(2) a security-based swap dealer or major security-based swap participant; or

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with the security-based swap." A "direct counterparty" is a person that is a primary obligor on a security-based swap. See Exchange Act rule 900(k) (defining "direct counterparty").

265 See rule 908(a). We also simultaneously proposed certain amendments to Regulation SBSR. See Regulation SBSR—Reporting and Dissemination of Security-Based Swap Information; Proposed Rule ("Regulation SBSR Proposed Amendments Release"), Exchange Act Release No. 74245 (February 11, 2015), 80 FR 14739 (March 19, 2015). These proposed amendments generally address issues separate from those being addressed in this release.

266 See Regulation SBSR Adopting Release, 80 FR 14655.

(3) a counterparty to a transaction conducted within the United States.[267]

Our recently adopted rule 908(b) included only the first two of these prongs, and the Regulation SBSR Adopting Release clarified that a security-based swap dealer or major security-based swap participant that is not a U.S. person would incur an obligation under Regulation SBSR only if it is registered.[268] We noted that we anticipated soliciting additional public comment on whether regulatory reporting and/or public dissemination requirements should be extended to transactions occurring within the United States between non-U.S. persons and, if so, which non-U.S. persons should incur reporting duties under Regulation SBSR.[269]

Finally, in the Cross-Border Proposing Release, we re-proposed rule 901(a), which set forth a reporting hierarchy for identifying which side has a duty to report in a variety of transactions. This rule would have provided, among other things, that, in a transaction in which neither side included a security-based swap dealer or major security-based swap participant, if one side included a U.S. person while the other side did not, the side with the U.S. person would have been the reporting side; if both sides in such transaction included a U.S. person or neither side included a U.S. person, the sides would have been required to select the reporting side.[270] In the Regulation SBSR Adopting Release, we adopted rules establishing the reporting hierarchy for a range of transactions, including a provision that, in a transaction in which neither side includes a registered security-based swap dealer or registered major security-based swap participant but both sides include a U.S. person, the sides shall select the reporting side.[271] We

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267 See Cross-Border Proposing Release, 78 FR 31065.

268 See rule 908(b); Regulation SBSR Adopting Release, 80 FR 14656.

269 See Regulation SBSR Adopting Release, 80 FR 14655.

270 See Regulation SBSR Adopting Release, 80 FR 14597.

271 See rule 901(a)(2)(ii)(E)(1).

noted in that release that we anticipated soliciting additional comment about how to apply Regulation SBSR, including which side should incur the reporting duty, in transactions between two unregistered non-U.S. persons and transactions between an unregistered U.S. person and an unregistered non-U.S. person.[272]

C. Commenters' Views

1. General comments on application of clearing, trade execution, regulatory reporting, and public dissemination requirements

One commenter generally supported our proposed territorial approach to applying these requirements, noting that the requirements "would encompass any transaction with a U.S. person or within the U.S."[273] Similarly, another market participant agreed with our proposed application of these requirements to security-based swaps entered into by offshore funds that have a U.S. nexus, arguing that a failure to apply such requirements would undermine central objectives of the Dodd-Frank Act, create opportunities for regulatory arbitrage, and risk fragmenting the security-based swap market.[274]

At the same time, other commenters raised concerns about our proposed approach.[275] Some commenters explained that applying mandatory clearing, mandatory trading, regulatory reporting, and public dissemination requirements to transactions between non-U.S. branches of

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272 See Regulation SBSR Adopting Release, 80 FR 14598.

273 Better Markets Letter at 19-20.

274 See Citadel Letter at 1.

275 See, e.g., IIB Letter at 6-7, 23 (stating that the registration requirement, external business conduct standards, clearing, trade execution, regulatory reporting, and public dissemination requirements should not apply to transactions of non-U.S. persons with foreign security-based swap dealers based on conduct in the United States when neither counterparty's obligations under the security-based swap are guaranteed by a U.S. person, because such an application would create "serious operational, legal and economic difficulties for foreign security-based swap market participants").

two U.S. persons would lead to duplication of, and conflicts with, foreign requirements.[276] Another commenter criticized the proposed approach to categorization of these requirements, stating that the proposal did not classify regulatory reporting, public dissemination, mandatory clearing, or mandatory trade execution as either entity-level requirements or transaction-level requirements but as a distinct category of "transactional requirements" that apply to persons regardless of their registration status.[277] This commenter argued that multiple categories of requirements make it more difficult for market participants to determine which requirements apply and whether substituted compliance is available.[278] The commenter contended that it would be simpler and more rational to apply the clearing, trade execution, regulatory reporting, and public dissemination requirements in the same way that we proposed to apply the external business conduct requirements.[279]

2. Comments on mandatory clearing and mandatory trade execution

Market participants expressed a range of views regarding the application of mandatory clearing and mandatory trade execution to transactions of non-U.S. persons conducted within the United States. One commenter supported our proposed definition of "transaction conducted within the United States" together with our proposal to impose the clearing requirement on such transactions because this approach would help ensure that the security-based swap activity of offshore funds managed by U.S.-based investment managers is subject to our clearing requirements.[280] Two commenters specifically argued that the proposed exceptions from the

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276 See IIB Letter at 9; EC Letter at 2.

277 See SIFMA/FIA/FSR Letter at A-38 to A-39.

278 See id.

279 See id.

280 See Citadel Letter at 3.

application of mandatory clearing should be eliminated,[281] and one commenter urged the same with respect to mandatory trade execution.[282] One of these commenters suggested that, at most, we should permit substituted compliance for the transactions rather than excepting them from any application of the clearing requirement.[283]

Other commenters opposed an activity-based application of mandatory clearing or trade execution. One market participant argued that conduct in the United States should not trigger the application of the clearing requirement because the test "is impractical, cannot be justified by cost-benefit analysis and exceeds the Commission's SBS authority under the Exchange Act."[284] Another commenter opposed applying regulatory requirements, including clearing and trade execution, to transactions between two unguaranteed non-U.S. persons that involve activity in the United States, regardless of their status as registered security-based swap dealers.[285]

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281 See AFR Letter at 10 (arguing that the exceptions were unreasonable because "no provision of Dodd-Frank justifies exempting security-based swaps that occur within our borders from U.S. regulatory requirements"); Better Markets Letter at 22 (arguing that the exception for the clearing requirement conflicts with the Commission's territorial approach). Cf. Letter from AFR to CFTC and SEC, dated November 25, 2014 (arguing that foreign subsidiaries of U.S. firms without guarantees may present risk to the United States).

282 See Better Markets Letter at 22.

283 See AFR Letter at 10.

284 See SIFMA/FIA/FSR Letter A-48. See also FOA Letter at 8 (stating that a transaction conducted within the United States that involves one non-U.S. person security-based swap dealer is insufficiently connected to the United States to require mandatory clearing and mandatory trade execution).

285 See ICI Letter at 8-10 n.23 (explaining that the risk in such transactions is outside the United States, that the counterparties would have no expectation that the requirements would apply, and that U.S. persons and non-U.S. persons that use U.S. asset managers would be placed at a competitive disadvantage); EC Letter at 2 (submitting that the Commission's rules should not apply to a transaction where the legal counterparty is a non-U.S. person, on the basis that there is no counterparty risk to a U.S. person in such a transaction).

3. Comments on regulatory reporting and public dissemination

Commenters expressed divergent views regarding application of Regulation SBSR to transactions involving the conduct of non-U.S. persons within the United States.[286] Noting its general opposition to the proposed "transaction conducted within the United States" concept, one commenter argued that the regulatory reporting and public dissemination requirements should not apply to transactions conducted within the United States between two non-U.S.-person counterparties because the proposed requirement would likely result in "duplicative reporting requirements."[287] Another commenter argued that it would be "unnecessary and unworkable" to require transactions that are between non-U.S. persons and are executed but not cleared in the United States to be reported, noting that such transactions would generally be subject to reporting in the counterparties' jurisdictions and additional reporting to a U.S. SDR would impose additional significant costs.[288] Another commenter argued that applying Regulation SBSR on the basis of conduct in the United States would not be workable because it would require a trade-by-trade analysis rather than "party level static data," for which system

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286 See Citadel Letter at 1-2; ABA Letter at 3 (noting that the initially proposed activity-based approach is consistent with longstanding Commission practice but also noting potential ambiguities); IAA Letter at 6 (explaining that the proposed term may capture parties with minimal connection to the United States); IIB Letter at 8-9 (explaining that application of the term may result in duplicative and conflicting regulation); EC Letter at 2 (explaining that the Commission's rules should not apply because no U.S. firms are subject to counterparty credit risk in such transactions); FOA Letter at 7-8 (explaining that the test would reach transactions with minimal nexus to the United States); JFMC Letter at 4-5 (requesting that the Commission not apply its rules to such transactions based on its belief that such an approach would conflict with the CFTC approach).

287 SIFMA/FIA/FSR Letter at A-42.

288 Letter from Cleary Gottlieb Steen & Hamilton LLP to CFTC, SEC, Board of Governors of the Federal Reserve System, Office of the Comptroller of the Currency, Federal Deposit Insurance Corporation, Federal Housing Finance Agency, and Farm Credit Administration ("Cleary Letter"), dated September 20, 2011 at 28 (suggesting that the Commission adopt accommodations for the use of non-U.S. SDRs in appropriate cases).

architecture does not currently exist.[289] This commenter also stated that market participants do not have the capability to determine whether their counterparty's activities trigger the proposed conduct test.[290]

4. The CFTC Staff Advisory and responses to the CFTC Request for Comment

As noted above, in response to the solicitation of comment on the CFTC Staff Advisory, commenters raised concerns specifically with respect to the application of the approach in that document to the CFTC's transaction-level requirements.

Some commenters suggested that only those CFTC transaction-level requirements directly relevant to the specific activities that the swap dealer carries out from a U.S. location should apply to the transaction, generally taking the view that the CFTC's regulatory interest extends only to counterparty-facing activities and not, for example, to the risk-mitigation aspects of Title VII.[291] One commenter suggested, however, that certain counterparty-facing

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[289] See Letter from ISDA to SEC dated November 14, 2014 ("ISDA Letter") at 18 (urging us not to apply Regulation SBSR on the basis of conduct within the United States as it would not be practicable). This commenter also argued that counterparties to a transaction executed on an SB SEF, and not the SB SEF itself, should be required to report such transactions. See id. at 7. See also Regulation SBSR Proposed Amendments Release, 80 FR 14748-49 (citing additional comment letters addressing this issue).

[290] See ISDA Letter at 18. This commenter also argued that, because in its view a security-based swap involving only non-U.S. persons that are not registered as a security-based swap dealer or as a major security-based swap participant should not be required to be reported, the reporting hierarchy need not address the reporting obligations arising from such security-based swap transactions. See id. at 19.

[291] See IIB Letter to CFTC at 8-10 (arguing that, if the CFTC adopts the CFTC Staff Advisory, it should apply only the transaction-level requirements relevant to the activity that occurs within the United States); SIFMA/FIA/FSR Letter to CFTC at A-9 to A-11 (any approach adopted by the CFTC that is based on the use of personnel located in the United States should trigger only requirements that relate to concerns raised by the conduct that triggered the requirements); Barclays Letter to CFTC at 3 (arguing that the only transaction-level requirements whose objectives are implicated by activity in which the "sole nexus to the U.S. is the participation of U.S.-based personnel of a non-U.S. swap dealer" are requirements related to "sales practices" and that, therefore, the only relevant transaction-level requirements that should apply to such transactions, should the CFTC adopt an approach that is based on the use of personnel located in the United States, are pre-trade disclosure requirements); ISDA Letter to CFTC at 9 (suggesting

communications raise no concerns relevant to Title VII and therefore should not trigger application of transaction-level requirements, even if a swap dealer engages in such communications within the United States.[292] Another commenter noted that this approach would help ensure that costs and benefits of such an approach were commensurate.[293]

Commenters also noted that a non-U.S.-person swap dealer using personnel or agents located in the United States to arrange, negotiate, or execute swap transactions generally would already be subject to regulation in its home jurisdiction.[294] In their view, adoption of the CFTC Staff Advisory would raise the possibility of conflicting and duplicative regulation of such non-U.S.-person swap dealers and reflected a lack of comity on the CFTC's part toward regulators in other jurisdictions.[295]

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that, should the CFTC adopt the approach in the CFTC Staff Advisory, only those transaction-level requirements that are transaction-specific and that relate to the triggering communication—transaction specific disclosure and communications—should apply to the transaction).

292 See SIFMA/FIA/FSR Letter at A-11 to A-12 (stating that "arranging and negotiating trading relationships and legal documentation and providing legal advice as well as providing credit terms and technical terms, market color, market research or a general discussion of the swap transaction" have no relation to any concerns of the Dodd-Frank Act in transactions between two non-U.S. persons).

293 See Barclays Letter to CFTC at 3.

294 See CDEU Letter to CFTC at 2, 3 (arguing that the approach in the CFTC Staff Advisory represents a departure from the CFTC Cross-Border Guidance in that a transaction between two entities organized under German law would be subject to the Title VII requirements and the EMIR requirements, which would be duplicative and unnecessary, without any ability for substituted compliance); IIB Letter to CFTC at 5 (explaining that "[i]t would stand international comity on its head for the [CFTC]" to adopt the CFTC Staff Advisory's approach of imposing regulatory requirements on non-U.S. firms on the basis of "limited activities" of their U.S. personnel or agents when the foreign jurisdiction has strong supervisory interests in the risks arising from the transactions); JFMC Letter to CFTC at 1 (explaining that the CFTC Staff Advisory's approach to applying transaction-level requirements does not account for the application of foreign regimes to the transaction).

295 See SIFMA/FIA/FSR Letter to CFTC at A-6 (explaining that the CFTC Staff Advisory fails to respect comity principles because it would not "give due recognition to the compelling supervisory interests of home regulators in the jurisdictions in which these transactions occur"). See also IIB Letter to CFTC at 6 (arguing that Dodd-Frank incorporates mechanism for addressing competition concerns: a "mandate" for international harmonization). Accordingly,

Some commenters suggested that adoption of the CFTC Staff Advisory could present difficulties for, and impose costs on, non-U.S.-person counterparties of dealers, as such counterparties may not currently have systems in place for complying with certain CFTC requirements, particularly if they are imposed only because the swap dealer (and not the counterparty) happens to have carried out certain activities using personnel or agents located in the United States.[296] As a result, commenters argued that non-U.S. swap dealers may no longer be able to service non-U.S.-person counterparties from U.S. locations.[297] Some commenters noted possible competitive effects of imposing, or not imposing, transaction-level requirements on such transactions. One commenter supported the CFTC Staff Advisory, arguing that without it, U.S. firms would be at a competitive disadvantage compared to non-U.S. firms operating in the United States, because U.S. firms would be subject to different rules for the same transactions.[298]

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they urged the CFTC to make substituted compliance available in such transactions. See CDEU Letter to CFTC at 5 (urging the CFTC to make substituted compliance determinations with respect to the transaction-level requirements and to defer to foreign regulators to regulate entities that are organized under the laws of their jurisdiction); ISDA Letter to CFTC at 4 (arguing that substituted compliance should be available for transactions between a non-U.S. swap dealer and a non-U.S. counterparty if the CFTC adopts the approach in the CFTC Staff Advisory); SIFMA/FIA/FSR Letter to CFTC at A-13 (suggesting that substituted compliance be available for the transaction-level requirements).

296 See, e.g., SIFMA/FIA/FSR Letter to CFTC at A-4 (explaining that certain non-U.S.-person counterparties may not have clearing relationships with FCMs, and requiring them to clear through an FCM simply because the dealer happens to use personnel within the United States in the transaction would be costly).

297 See, e.g., ISDA Letter to CFTC at 4.

298 See AFR Letter to CFTC at 3 (explaining that "any weakening of [the] advisory would open the door to regular and significant levels of swaps activities being performed within the U.S. by nominally foreign entities under foreign rules, or in some cases no rules at all," whereas U.S. firms operating in the United States would be subject to different rules for the same transactions operating in the same market).

Some commenters indicated that adoption of the CFTC Staff Advisory would also disadvantage non-dealing counterparties. For example, one commenter argued that, were the CFTC Staff Advisory adopted, end users that trade with non-U.S. swap dealers might face competitive disadvantages.[299] Other commenters noted that the application of transaction-level requirements to such transactions could put foreign swap dealers at a competitive disadvantage because it would be overly burdensome for them to use U.S.-based personnel or agents to perform certain function in connection with their dealing activity, particularly with respect to transactions with foreign counterparties that may oppose being subject to transaction-level requirements, and that the adoption of the CFTC Staff Advisory would therefore encourage dealers not to use their U.S.-based personnel.[300]

D. Mandatory Clearing and Trade Execution

After careful consideration of concerns raised by commenters and our further consideration of policy concerns relevant to the security-based swap market, we are not proposing to subject transactions between two non-U.S. persons to the clearing requirement (and,

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299 See CDEU Letter to CFTC at 2 (urging the CFTC not to adopt the Staff Advisory because it would lead to competitive disadvantages for certain non-U.S. end-user affiliates that had relied on trading with non-U.S. swap dealers compared to other non-U.S. end users in the same markets that currently hedge with unregistered counterparties). This commenter also expressed concern that applying the transaction-level requirements to such transactions would disadvantage non-U.S.-person non-dealers that choose to hedge with non-U.S. swap dealers using personnel or agents in the United States, as compared to non-U.S. persons that choose to hedge with unregistered counterparties or dealers that do not use personnel or agents in the United States. See CDEU Letter to CFTC at 1-2.

300 See ISDA Letter to CFTC at 4 (noting that non-U.S. counterparties have insisted that a swap dealer not use its U.S.-based personnel so as to avoid being subject to transaction-level requirements). See also JFMC Letter to CFTC at 1 (explaining that adoption of the CFTC Staff Advisory would create regulatory uncertainty and disrupt the planning of firms' systems and put Asia-based swap dealers at a disadvantage if they want to use U.S.-based personnel or agents).

by extension, to the trade execution requirement[301]) on the basis of dealing activity in the United States, including transactions that are arranged, negotiated, or executed by personnel located in a U.S. branch or office.

As we noted in the Cross-Border Proposing Release, because the financial risks of such a transaction reside outside the United States, "it is not necessary to apply the mandatory clearing requirement to a transaction between two non-U.S. persons solely" because the transaction involves activity in the United States.[302] However, the proposed approach would have subjected a "transaction conducted within the United States" involving at least one registered foreign security-based swap dealer to the clearing requirement (and, as noted, to the trade execution requirement). We proposed this approach because we preliminarily believed that registered foreign security-based swap dealers would have a more significant connection to the United States and to minimize potential competitive disparities between U.S. persons and non-U.S. persons.[303]

On further consideration, however, we now preliminarily believe that we should not impose the clearing requirement on a security-based swap transaction between two non-U.S. persons where neither counterparty's obligations under the security-based swap are guaranteed by a U.S. person, even if the transaction involves one or more registered foreign security-based swap dealers. In our view, a key objective of the clearing requirement is to mitigate systemic

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301 We continue to believe that, under the statutory framework, a security-based swap transaction is potentially subject to the trade execution requirement only if it is first subject to the clearing requirement. See Cross-Border Proposing Release, 78 FR 31082. Accordingly, to the extent that the clearing requirement does not apply to a particular security-based swap transaction, the trade execution requirement also would not apply. See id. (noting that, to the extent that we are proposing not to apply the clearing requirement to a particular transaction, the trade execution requirement would not apply to such transaction).

302 Cross-Border Proposing Release, 78 FR 31080.

303 See id. at 31080.

and operational risk in the United States, but the counterparty credit risk and operational risk of such transactions reside primarily outside the United States.[304] Accordingly, we preliminarily believe that subjecting such security-based swaps to the clearing requirement would not significantly advance what we view as a key policy objective of the clearing requirement applicable to security-based swaps under the Dodd-Frank Act.[305]

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304 See id. at 31077; note 285, supra (citing EC Letter arguing that activity between two non-U.S. persons in the United States does not create counterparty credit risk in the United States). We recognize that even if a transaction involving one or more registered foreign security-based swap dealers that is arranged, negotiated, or executed by personnel located in the United States does not create financial or counterparty credit risk that resides in the United States, it may create operational risks associated, for example, with the processing of the transaction. See id. However, such risks are borne primarily by the counterparties to the transaction, both of whom are by definition—in the transactions being addressed in this release—non-U.S. persons (because they are incorporated outside the United States and do not have their principal place of business in the United States). Accordingly, any reduction of operational risks in the U.S. financial market that would be produced by requiring these transactions to be cleared by a U.S.-registered clearing agency would likely be insignificant. On the other hand, imposing the clearing requirement on a transaction between two non-U.S. persons involving at least one registered foreign security-based swap dealer because the transaction was arranged, negotiated, or executed in the United States to be cleared by a U.S.-registered clearing agency would directly expose that clearing agency and, through it, the U.S. financial system to the counterparty credit risk of the transaction.

305 For these reasons, we disagree with commenters that characterized any exception from the clearing requirement as "indefensible" or "unreasonable." See note 281, supra.

We recognize that another commenter suggested that our initially proposed approach, which would have required a "transaction conducted within the United States" to be cleared, subject to certain exceptions, would help ensure that transactions of non-U.S.-person funds that are managed by U.S.-based investment managers are subject to the Title VII clearing requirement. See note 280, supra (citing Citadel Letter). Under the approach set forth in this release, the transactions of such funds may not be subject to the clearing requirement when the counterparty is not a U.S. person, but, as already noted, the risks of such transactions reside primarily outside the United States, and we preliminarily do not believe that requiring such transactions to be cleared would further the purposes of the clearing requirement. To the extent that the fund has its principal place of business in the United States, of course, it would be a U.S. person and, under the approach set forth in our Cross-Border Proposing Release, would be subject to the clearing requirement. See Exchange Act rule 3a71-3(a)(4)(B) (defining "U.S. person" to include, among other things, an investment vehicle "having its principal place of business in the United States"); Cross-Border Proposing Release, 78 FR 31078 (describing applicability of clearing requirement to U.S. persons under that proposal). Cf. note 285, supra (citing ICI Letter noting that mere presence of an investment manager in the United States does not necessarily create risk in the United States).

We recognize that, to the extent that a non-U.S. person using personnel located in a U.S. branch or office to arrange, negotiate, or execute security-based swap transactions in connection with its dealing activity is affiliated with a U.S. financial firm, the non-U.S. person's security-based swap exposures may pose risk to its U.S. affiliates in the United States, as U.S. entities that are affiliated with non-U.S. persons may determine for reputational reasons that they must support their non-U.S. affiliates at times of crisis.[306] However, as we noted in the Cross-Border Adopting Release, Congress has established other regulatory tools that are specifically intended, and better suited, to address risks to bank holding companies and financial holding companies, arising from the financial services activities of a foreign affiliate of those holding companies where the foreign affiliate does not engage in security-based swap activity in the United States,[307] and we preliminarily believe the same principle applies here. Moreover, we note that it is likely that such a non-U.S. person engaged in significant security-based swap dealing activity would be a registered security-based swap dealer under our proposed approach and subject to Title VII capital and margin requirements, which we preliminarily believe would be a more narrowly tailored and appropriate way of mitigating any such risk in this context.[308] Under proposed rule 3a71-3(b)(1)(iii)(C), the non-U.S. person would be required to include in its dealer de minimis threshold calculations any security-based swap transaction that it arranged, negotiated, or executed in connection with its dealing activity using personnel located in a U.S.

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306 See Cross-Border Adopting Release, 79 FR 47318. As we noted in the Cross-Border Adopting Release, however, any U.S. person that is subject to the reporting requirements of section 13(a) or section 15(d) of the Exchange Act, 15 U.S.C. 78m(a) or 15 U.S.C. 78o(d) respectively, regardless of whether that person provides a recourse guarantee relating to its non-U.S. affiliates' obligations, must consider whether there are disclosures that must be made in its periodic reports regarding any of its obligations. See Cross-Border Adopting Release, 79 FR 47318 n.348.

307 See id. at 47318-19.

308 We also note in this regard the relatively low liquidity of the security-based swap market in general, even for the most liquid products. See Section II.B.3, supra.

branch or office. Any non-U.S. person engaged in significant activity in the United States, including a non-U.S.-person affiliate of a U.S. financial firm whose obligations under a security-based swap are not guaranteed by its U.S. parent, would be required to register as a security-based swap dealer and comply with Title VII capital and margin requirements (along with other entity-level requirements). Whereas the clearing requirement would have applied only to certain transactions of registered foreign security-based swap dealers, capital and margin requirements would apply to all of their security-based swap transactions, including those that do not involve personnel located in a U.S. branch or office.[309]

We also preliminarily believe that requiring such security-based swap transactions to be cleared (and executed on a platform) would impose a significant burden on certain market participants. Some non-U.S. person counterparties may not currently have a direct or indirect relationship with a U.S.-registered clearing agency, and the burdens of establishing such a relationship may deter these non-U.S. persons—particularly those not engaged in dealing activity—from entering into security-based swap transactions with non-U.S. persons that, in connection with their dealing activity arrange, negotiate, or execute such transactions using personnel located in a U.S. branch or office.[310] Given that, under our proposed approach, a non-U.S. person that engages in significant security-based swap activity using personnel located in a U.S. branch or office is likely to be required to register and be subject to Title VII capital and

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309 See, e.g., Cross-Border Proposing Release, 78 FR 31011-12 (proposing to treat margin as an entity-level requirement).

310 See notes 296-297, supra. Establishing a direct relationship with a clearing agency may entail upfront costs that include, among other things, meeting minimum capital requirements and making minimum clearing fund contributions. See, e.g., ICE Clear Credit Clearing Rules at 12 and 90 (available at: https://www.theice.com/publicdocs/clear_credit/ICE_Clear_Credit_Rules.pdf, last visited April 15, 2015).

margin requirements with respect to all of its transactions, we preliminarily do not believe that subjecting a subset of these persons' activities to the clearing requirement is likely to provide a significant additional reduction in counterparty credit risk in the United States. Consistent with customary Commission practice, we expect that Commission staff will monitor developments in the security-based swap market, including changes in liquidity or market fragmentation, that may warrant reconsideration of this proposed approach and, if necessary and appropriate, make recommendations to address such developments.

Because such security-based swap transactions would not be subject to the clearing requirement, under our proposed approach they would also not be subject to mandatory trade execution. While we acknowledge that trading between two non-U.S. persons in the OTC market may indirectly affect liquidity available to market participants subject to mandatory trade execution,[311] we preliminarily do not believe that it is appropriate to require such non-U.S. persons to shift their non-U.S. business to trading platforms merely because one of the counterparties to the transaction uses personnel located in a U.S. branch or office to arrange, negotiate, or execute the transaction.[312] As with the clearing requirement, and consistent with customary Commission practice, we expect that Commission staff will monitor developments in the security-based swap market, including changes in liquidity or market fragmentation, that may warrant reconsideration of this proposed approach and, if necessary and appropriate, make recommendations to address such developments.

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311 See Section VI.C.4, infra.

312 See note 308, supra.

E. Regulation SBSR

We are proposing amendments to Regulation SBSR to address the application of the regulatory reporting and public dissemination requirements to certain transactions not addressed in the Regulation SBSR Adopting Release or the Regulation SBSR Proposed Amendments Release.

1. Statutory framework

Section 13A(a)(1) of the Exchange Act[313] provides that "[e]ach security-based swap that is not accepted for clearing by any clearing agency or derivatives clearing organization shall be reported to—(A) a registered security-based swap data repository described in section 13(n); or (B) in the case in which there is no security-based swap data repository that would accept the security-based swap, to the Commission." Section 13(m)(1)(G) of the Exchange Act[314] provides that "[e]ach security-based swap (whether cleared or uncleared) shall be reported to a registered security-based swap data repository."

Section 13(m)(1)(B) of the Exchange Act[315] directs the Commission "to make security-based swap transaction and pricing data available to the public in such form and at such times as the Commission determines appropriate to enhance price discovery." Section 13(m)(1)(C) of the Exchange Act[316] authorizes the Commission to provide by rule for the public availability of security-based swap transaction, volume, and pricing data. Furthermore, section 13(m)(1)(D) of the Exchange Act[317] authorizes the Commission to require registered entities (such as registered

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313 15 U.S.C. 78m-1(a)(1).

314 15 U.S.C. 78m(m)(1)(G). See also 15 U.S.C. 78q(a)(1).

315 15 U.S.C. 78m(m)(1)(B). See also 15 U.S.C. 78q(a)(1).

316 15 U.S.C. 78m(m)(1)(C).

317 15 U.S.C. 78m(m)(1)(D).

SDRs) to publicly disseminate the security-based swap transaction and pricing data required to be reported under section 13(m) of the Exchange Act. Finally, section 13(n)(5)(D)(ii) of the Exchange Act[318] requires SDRs to provide security-based swap information "in such form and at such frequency as the Commission may require to comply with the public reporting requirements."

In the Regulation SBSR Adopting Release, we interpreted the regulatory reporting and public dissemination requirements to apply to security-based swaps that "exist, at least in part, within the United States"[319] and noted that a security-based swap with a direct or indirect counterparty that is a U.S. person necessarily would exist within the United States.[320] This view is consistent with a territorial approach to the statutory language requiring the reporting of "[e]ach security-based swap," and with the statutory requirement that security-based swaps that are reported must be publicly disseminated, unless an exception applies.[321] In our view, it is also consistent with a territorial approach to these statutory provisions to require each security-based swap that is otherwise subject to regulatory requirements under Title VII (as implemented under our territorial approach to implementing those requirements) to be reported and publicly disseminated pursuant to Regulation SBSR.

2. Proposed amendments regarding application of Regulation SBSR to certain security-based swap transactions

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318 15 U.S.C. 78m(n)(5)(D)(ii).

319 See, e.g., Regulation SBSR Adopting Release, 80 FR 14651.

320 See Regulation SBSR Adopting Release, 80 FR 14650.

321 See Regulation SBSR Adopting Release, 80 FR 14649-50.

(a) Security-based swap transactions that a non-U.S. person, in connection with its dealing activity, arranges, negotiates, or executes using personnel located in a U.S. branch or office

We propose to amend rule 908(a)(1) of Regulation SBSR to include a provision that would require any security-based swap transaction connected with a person's security-based swap dealing activity that is arranged, negotiated, or executed by personnel of such non-U.S. person located in a U.S. branch or office—or by personnel of its agent located in a U.S. branch or office—to be reported to a registered SDR and publicly disseminated pursuant to Regulation SBSR.[322] This proposed amendment generally reflects the approach described in our Cross-Border Proposing Release, which would have subjected "transactions conducted within the United States" to both regulatory reporting and public dissemination requirements.[323] Consistent

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322 See proposed rule 908(a)(1)(v). We intend the proposed rule to indicate the same type of activity by personnel located in the United States as described in Section III.B.5, supra. Moreover, for purposes of proposed rule 908(a)(1)(v), we would interpret the term "personnel" in a manner consistent with the definition of "associated person of a security-based swap dealer" contained in section 3(a)(70) of the Exchange Act, 15 U.S.C. 78c(a)(70), regardless of whether such non-U.S. person or such non-U.S. person's agent is itself a security-based swap dealer. See note 193, supra (discussing the Commission's proposed interpretation of the term "personnel" for purposes of proposed rule 3a71-3(b)(1)(iii)(C)).

323 We preliminarily believe that the approach reflected in this release, which focuses only on whether a counterparty in connection with its dealing activity has arranged, negotiated, or executed the security-based swap transaction using personnel located in the United States, should mitigate many of the concerns raised by commenters. See note 286, supra (citing several comment letters arguing, among other things, that requirements, including Regulation SBSR, should not apply to transactions with only a minimal connection to the United States). See also notes 289-290, supra (citing comment letters arguing that looking to activity in the United States as a trigger for Regulation SBSR would not be practicable); note 292, supra (citing SIFMA/FIA/FSR Letter).

We recognize that some commenters suggested that certain Title VII requirements, including the regulatory reporting and public dissemination requirements implemented by Regulation SBSR, should not apply to transactions between two non-U.S. persons even if they involve activity in the United States because of operational complications or potential regulatory overlap or duplication. See note 275-276, 286-287, and 294-295, supra. We do not believe, however, that reporting a security-based swap to a registered SDR is likely to pose significant challenges, as the burden is borne under our rules only by one side of the transaction, and at least one counterparty to any transaction arranged, negotiated, or executed by a non-U.S. person, in connection with its dealing

with that approach, it would expand the scope of Regulation SBSR in two ways. First, it would require the security-based swaps that a registered foreign security-based swap dealer arranges, negotiates, or executes using personnel located in a U.S. branch or office to be publicly disseminated, even if the counterparty to such transaction is another non-U.S. person whose obligations under the security-based swap are not guaranteed by a U.S. person.[324] Second, it would require that a transaction of a non-U.S. person that is not a registered security-based swap dealer be subject to both regulatory reporting and public dissemination under Regulation SBSR if that non-U.S. person would be required to include the transaction in its de minimis threshold calculations under proposed Exchange Act rule 3a71-3(b)(1)(iii)(C), as described above.

Requiring these transactions to be reported to a registered SDR should enhance our ability to oversee relevant activity related to security-based swap dealing occurring within the United States as well as to monitor market participants for compliance with specific Title VII requirements (including the requirement that a person register with the Commission as a security-based swap dealer if it exceeds the de minimis threshold). We preliminarily believe it would also likely enhance our ability to monitor for manipulative and abusive practices involving security-based swap transactions or transactions in related underlying assets, such as

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activity, using personnel located in a U.S. branch or office is already likely to have infrastructure in place to report transactions to a registered SDR.

[324] Under Exchange Act rule 3a71-1(c), absent a limitation by the Commission, a security-based swap dealer is deemed to be a security-based swap dealer with respect to each security-based swap it enters into, regardless of the type, class, or category of the security-based swap or the person's activities in connection with the security-based swap. Accordingly, for purposes of this proposed amendment, any transaction that a registered security-based swap dealer arranged, negotiated, or executed using personnel located in a U.S. branch or office would be "in connection with its dealing activity" and subject to both regulatory reporting and public dissemination.

corporate bonds or other securities transactions that result from dealing activity, or other relevant activity, in the U.S. market.

Subjecting these transactions to the public dissemination requirements of Regulation SBSR should enhance the level of transparency in the U.S. security-based swap market, potentially reducing implicit transaction costs[325] and promoting greater price efficiency. As we noted in the Regulation SBSR Adopting Release, the current market for security-based swaps is opaque.[326] Dealers can observe order flow submitted to them by customers and other potential counterparties and know about their own executions, and may know about other dealers' transactions in certain instances, but information about executed transactions is not widespread. Market participants—particularly non-dealers—have to arrive at a price at which they would be willing to assume risk with little or no knowledge of how other market participants would or have arrived at prices at which they have assumed or would be willing to assume risk. We preliminarily believe that, by reducing information asymmetries between non-dealers and persons acting in a dealing capacity and providing more equal access to post-trade information in the security-based swap market, implicit transaction costs could be reduced, which could in turn promote greater price efficiency.[327] Ensuring that post-trade information encompasses

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325 As discussed in the Regulation SBSR Adopting Release, dealing activity in the single-name CDS market is concentrated among a small number of firms that each enjoy informational advantages as a result of the large quantity of order flow they privately observe. Implicit transaction costs are the difference between the transaction price and the fundamental value, which could reflect adverse selection or could reflect compensation for inventory risk. In addition to these implicit transaction costs, security-based swap market participants may face explicit transaction costs such as commissions and other fees that dealers might charge non-dealers for access to the market. See Regulation SBSR Adopting Release, 80 FR 14704 n.1254.

326 See Regulation SBSR Adopting Release, 80 FR 14605.

327 Security-based swaps are complex derivative products, and there is no single accepted way to model a security-based swap for pricing purposes. As we noted in the Regulation SBSR Adopting Release, making post-trade pricing and volume information publicly available should allow valuation models to be adjusted to reflect how other market participants have valued a

transactions involving a non-U.S. person that arranged, negotiated, or executed the security-based swap in connection with its dealing activity using personnel located in a U.S. branch or office could increase price competition and price efficiency in the security-based swap market and should enable all market participants to have more comprehensive information with which to make trading and valuation determinations.[328]

(b) Security-based swaps executed on a platform having its principal place of business in the United States

We also are proposing to amend rule 908(a)(1) of Regulation SBSR by adding a provision that would require any security-based swap transaction that is executed on a platform[329] having its principal place of business in the United States both to be reported to a registered SDR and to be publicly disseminated pursuant to Regulation SBSR.[330] Under our previously re-proposed rule, such transactions generally would have been subjected to Regulation SBSR as "transactions conducted within the United States" under the proposed definition of that term.

As noted above, our proposed amendments to Regulation SBSR focus on transactions that a non-U.S. person, in connection with its dealing activity, arranges, negotiates, or executes

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security-based swap product at a specific moment in time. Public dissemination of last-sale information also should aid persons engaged in dealing activity in deriving better quotations, because they will know the prices at which other market participants have traded. Last-sale information also should aid end users and other non-dealing entities in evaluating current quotations, by allowing them to question why a dealer's quote differs from the prices of the most recent transactions. Furthermore, smaller market participants that view last-sale information should be able to test whether quotations offered by dealers before the last sale were close to the price at which the last sale was executed. In this manner, post-trade transparency should promote price competition and more efficient price discovery in the security-based swap market. See Regulation SBSR Adopting Release, 80 FR 14606.

328 See id.

329 Regulation SBSR defines "platform" to mean "a national securities exchange or security-based swap execution facility that is registered or exempt from registration." Rule 900(v).

330 See proposed rule 908(a)(1)(iii).

using personnel located in a U.S. branch or office rather than on the broader range of activity reflected in our proposed definition of "transaction conducted in the United States." We preliminarily continue to believe, however, that a transaction executed on a platform that has its principal place of business in the United States also should be subject to Regulation SBSR, even when the transaction involves two non-U.S. persons that are not engaged in dealing activity in connection with the transaction. Transactions executed on a platform having its principal place of business in the United States are consummated within the United States and therefore exist, at least in part, in the United States.[331] Requiring these security-based swaps to be reported to a registered SDR will permit the Commission and other relevant authorities to observe, in a registered SDR, all transactions executed on such a platform and to carry out oversight of such security-based swaps. Furthermore, we preliminarily believe that public dissemination of such transactions would have value to participants in the U.S. security-based swap market, who are likely to trade the same or similar products, as these products will have been listed by a platform having its principal place of business in the United States.

(c) Security-based swaps effected by or through a registered broker-dealer

We are also proposing to amend rule 901(a) of Regulation SBSR by adding a provision that would require the reporting and public dissemination of any security-based swap transaction

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[331] Cf. Regulation SBSR Adopting Release, 80 FR 14654 (noting that a security-based swap that is accepted for clearing by a clearing agency having its principal place of business in the United States also exists, at least in part, within the United States).

Requiring these transactions to be reported should enable registered SDRs to have a complete record of all security-based swaps that are executed on platforms that have their principal place of business in the United States, which should enhance our ability to monitor these platforms, and activity in the security-based swap market more generally, for manipulation and other abusive practices. Cf. Cross-Border Proposing Release, 78 FR 31040 (noting importance of having a complete record of security-based swaps). Requiring these transactions to be reported should also enhance our ability to monitor activity on these platforms for compliance with recordkeeping and reporting and other requirements. See Cross-Border Proposing Release, 78 FR 31183 (discussing the market-wide benefits of enhanced transparency).

that is effected by or through a registered broker-dealer (including a registered SB SEF).[332] As noted above, existing rule 908(a)(1) already provides that any transaction involving a U.S. person, either directly or indirectly, on one or both sides of the transaction subjects that transaction to both regulatory reporting and public dissemination; proposed rule 908(a)(1)(v) would impose the same requirements with respect to any transaction that a non-U.S. person in connection with its dealing activity arranges, negotiates, or executes using its personnel or the personnel of its agent located in a U.S. branch or office. Given the limitation on reporting duties set forth in rule 908(b) and in the proposed amendments to that rule, we expect that most, if not all, registered broker-dealers required to report under this proposed amendment would be U.S. persons intermediating security-based swap transactions between non-U.S. person counterparties and that such persons would be effecting transactions in security-based swaps from their offices in the United States. Moreover, under the proposed amendments to the reporting hierarchy described below, a registered broker-dealer (including a registered SB SEF) would be required to report transactions effected by or through it only when neither side of that transaction includes a U.S. person, neither side is a registered security-based swap dealer or registered major security-based swap participant, and neither side of that transaction involves a non-U.S. person that has, in connection with its dealing activity, arranged, negotiated, or executed the security-based swap using its personnel or the personnel of its agent located in a U.S. branch or office.[333]

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332 See proposed rule 908(a)(1)(iv).

333 We acknowledge that some commenters urged us not to require SB SEFs to report transactions under Regulation SBSR. See note 289, supra. We preliminarily believe, however, that a registered broker-dealer (including a registered SB SEF) is likely to be better positioned to report than either counterparty to a transaction described in proposed rule 901(a)(2)(ii)(E)(4). We note that proposed rule 901(a)(2)(ii)(E)(4) applies only when two non-U.S. persons who are not registered security-based swap dealers, registered major security-based swap participants, or non-U.S. persons that fall within proposed rule 908(b)(5) effect a security-based swap through a registered broker-dealer. In the Regulation SBSR Adopting Release, we observed that non-

To the extent that a registered broker-dealer intermediates a security-based swap transaction, we preliminarily believe that the transaction should be both reported to a registered SDR and publicly disseminated. Registered broker-dealers play a key role as intermediaries in the U.S. financial markets. To improve integrity and transparency in those markets, we believe that it is important that the Commission, and other relevant authorities, have ready access to detailed information about the security-based swap transactions that such persons intermediate. Furthermore, we preliminarily believe that public dissemination of such transactions will have value to participants in the U.S. security-based swap market, who are likely to trade the same or similar products.

3. Application of the public dissemination requirement to certain transactions

In the Regulation SBSR Adopting Release, we adopted rule 908(a)(1)(i), which requires, among other things, public dissemination of all security-based swap transactions having a U.S.-person guarantor, including transactions in which the other side includes no counterparty that is a U.S. person, registered security-based swap dealer, or registered major security-based swap participant (a "covered cross-border transaction").[334] This represented a departure from the re-proposed approach described in the Cross-Border Proposing Release, which would have excepted covered cross-border transactions from the public dissemination requirement.[335] We

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registered persons are less likely than Commission registrants to have systems in place to support the reporting required by Regulation SBSR, and we preliminarily believe that the same applies here. See Regulation SBSR Adopting Release, 80 FR 14600.

334 See rule 908(a)(1)(i); Regulation SBSR Adopting Release, 80 FR 14652-53. As in the Regulation SBSR Adopting Release, a "covered cross-border transaction" refers to a transaction that meets the description above and will not be submitted to clearing at a registered clearing agency having its principal place of business in the United States. See Regulation SBSR Adopting Release, 80 FR 14653.

335 See Cross-Border Proposing Release, 78 FR 31062; initially re-proposed rule 908(a)(2) (requiring that security-based swaps be publicly disseminated if there is a direct or indirect counterparty that is a U.S. person on each side of the transaction).

noted, however, that we had determined to continue considering whether to except covered cross-border transactions from the public dissemination requirement and that we would solicit additional comment regarding whether such an exception would be appropriate. We solicit comment on this approach in the request for comments below.

In light of our determination to require all security-based swap transactions of U.S. persons, including all transactions conducted through a foreign branch, to be publicly disseminated, we preliminarily do not think that it would be appropriate to exempt covered cross-border transactions from the public dissemination requirement. As we have noted elsewhere, the transactions of a guaranteed non-U.S. person exist, at least in part, within the United States, and the economic reality of these transactions is substantially identical to transactions entered into directly by a U.S. person (including through a foreign branch).[336] Failure to require such transactions to be publicly disseminated would treat these economically substantially identical transactions differently, potentially creating competitive disparities between U.S. persons, depending on how they have structured their business, as a guaranteed non-U.S. person would be able to carry out an unlimited volume of covered cross-border transactions without being subject to the public dissemination requirement.[337]

4. Proposed amendments regarding limitations on reporting obligations of certain persons engaged in security-based swaps subject to Regulation SBSR

Rule 908(b) of Regulation SBSR provides that, notwithstanding any other provision of Regulation SBSR, a person shall not incur any obligation under Regulation SBSR unless it is a

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336 See note 319, supra.

337 However, if the transactions of a guaranteed non-U.S. person are subject to regulatory reporting and public dissemination requirements in a foreign jurisdiction that are comparable to those imposed by Regulation SBSR, such transactions could be eligible for substituted compliance. See rule 908(c).

U.S. person, a registered security-based swap dealer, or a registered major security-based swap participant.[338] We noted that rule 908(b) is designed to specify the types of persons that will incur duties under Regulation SBSR. If a person does not come within any of the categories enumerated by rule 908(b), it would not incur any duties under Regulation SBSR.[339] Rule 908(b) was designed to reduce assessment costs and provide greater legal certainty to counterparties engaging in cross-border security-based swaps, and we explained that we anticipated soliciting additional public comment regarding whether regulatory reporting and/or public dissemination requirements should be extended to transactions between non-U.S. persons occurring within the United States and, if so, which non-U.S. persons should incur reporting duties under Regulation SBSR.[340]

Consistent with the proposed amendments described above, and so that at least one counterparty to a transaction that is subject to Regulation SBSR has an obligation to report the transaction to a registered SDR, we are proposing to add subparagraph (5) to rule 908(b) to include a non-U.S. person that, in connection with such person's security-based swap dealing activity, arranged, negotiated, or executed the security-based swap using its personnel located in a U.S. branch or office, or using personnel of its agent located in a U.S. branch or office.[341]

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338 See rule 908(b). In the Regulation SBSR Proposed Amendments Release, we proposed to amend rule 908(b) by adding platforms and registered clearing agencies to the list of persons that might incur obligations under Regulation SBSR. See Regulation SBSR Proposed Amendments Release, 80 FR 14759.

339 See Regulation SBSR Adopting Release, 80 FR 14656.

340 See id.

341 See proposed rule 908(b)(5). We intend the proposed rule to indicate the same type of activity by personnel located in the United States as described in Section III.B.5, supra. Moreover, for purposes of proposed rule 908(b)(5), we would interpret the term "personnel" in a manner consistent with the definition of "associated person of a security-based swap dealer" contained in section 3(a)(70) of the Exchange Act, 15 U.S.C. 78c(a)(70), regardless of whether such non-U.S. person or such non-U.S. person's agent is itself a security-based swap dealer. See note 193, supra

Because existing rule 908(b)(2) already covers a non-U.S. person that is registered as a security-based swap dealer, the effect of proposed rule 908(b)(5) would be to cover a non-U.S. person that engages in dealing activity in the United States but that does not meet the de minimis threshold and thus would not be registered as a security-based swap dealer.

5. Proposed amendment regarding reporting duties of certain persons that are not registered security-based swap dealers or registered major security-based swap participants

Rule 901(a)(2)(ii) of Regulation SBSR establishes a reporting hierarchy that specifies the side that has the duty to report a security-based swap, taking into account the types of entities present on each side of the transaction.[342] The reporting side, as determined by the reporting hierarchy, is required to submit the information required by rule 901 of Regulation SBSR to a registered SDR.[343] The reporting side may select the registered SDR to which it makes the required report.

Rule 901(a)(2) of Regulation SBSR does not assign reporting obligations for certain transactions having only unregistered entities on both sides of the transaction. In the Regulation SBSR Adopting Release, we specifically noted that we anticipated soliciting further comment regarding the duty to report a security-based swap where neither side includes a registered security-based swap dealer or a registered major security-based swap participant and neither side includes a U.S. person or only one side includes a U.S. person.[344] In this release we are

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(discussing the Commission's proposed interpretation of the term "personnel" for purposes of proposed rule 3a71-3(b)(1)(iii)(C)).

342 See rule 901(a).

343 Rule 900(gg) defines "reporting side" to mean "the side of a security-based swap identified by § 242.901(a)(2)." As noted above, rule 901(a)(2) identifies the person that will be obligated to report a security-based swap under various circumstances.

344 See Regulation SBSR Adopting Release, 80 FR 14600, 14655.

proposing additional provisions setting forth which sides would have the duty to report such transactions.

As noted above, and as discussed in the Regulation SBSR Adopting Release, one commenter raised concerns about burdens that the previously re-proposed reporting hierarchy might place on U.S. persons in transactions with certain non-U.S.-person counterparties.[345] Under that approach, in a transaction between a non-U.S. person and a U.S. person, where neither side included a security-based swap dealer or major security-based swap participant, the U.S. person would have had the duty to report. The commenter noted that in such transactions the non-U.S.-person counterparty might be engaged in dealing activity but at levels below the security-based swap dealer de minimis threshold and the U.S. person may not be acting in a dealing capacity in any of its security-based swap transactions. The commenter argued that, in such cases, the non-U.S. person may be better equipped to report the transaction and accordingly that, when two non-registered persons enter into a security-based swap, the counterparties should be permitted to select which counterparty would report, even if one counterparty is a U.S. person.[346]

Proposed rule 901(a)(2)(ii)(E)(2) is intended in part to address this concern when the non-U.S. person is engaged in dealing activity using personnel located in the United States. Under the proposed rule, in a transaction between such a non-U.S. person and a U.S. person, where neither side includes a registered security-based swap dealer or a registered major security-based swap participant, the sides would be permitted to select which side has the duty to

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345 See IIB Letter at 26; Regulation SBSR Adopting Release, 80 FR 14600.

346 See IIB Letter at 26 (stating that, in such transactions, "it would be more efficient and fair for the Commission to modify its rules to allow a De Minimis SBSD to agree with its counterparty to be the reporting party when facing a U.S. non-registrant counterparty").

report the transaction.[347] We preliminarily believe that this approach should facilitate efficient allocation of reporting duties between the sides by permitting the counterparties to select the reporting side.

For similar reasons, proposed rule 901(a)(2)(ii)(E)(2) also provides that, in a transaction between two non-U.S. persons in which both sides include a non-U.S. person that is carrying out relevant security-based swap dealing activity using personnel located in a U.S. branch or office, as described in proposed rule 908(b)(5), the sides would be permitted to select which side has the duty to report the transaction. We preliminarily believe that, because both sides of such a transaction are engaging in dealing activity in the United States but both fall beneath the de minimis thresholds, both sides are likely to have approximately equivalent levels of infrastructure to support their U.S. business, including the infrastructure for reporting transactions to a registered SDR. In such cases, we preliminarily believe that it would be reasonable and appropriate to permit them to select which side will have the duty to report.[348]

With respect to transactions in which one side includes only unregistered non-U.S. persons that do not fall within proposed rule 908(b)(5) and the other side includes at least one unregistered non-U.S. person that does fall within proposed rule 908(b)(5) or one unregistered U.S. person, we preliminarily believe that it is appropriate to place the reporting duty on the side that includes the unregistered non-U.S. person that falls within proposed rule 908(b)(5) or the

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347 See proposed rule 901(a)(2)(ii)(E)(2).

348 Similar considerations have informed our proposal to permit counterparties to a transaction where both sides include only non-U.S. persons that do not fall within proposed rule 908(b)(5) to select the reporting side. See proposed rule 901(a)(2)(ii)(E)(4). Such a transaction would be subject to Regulation SBSR because it has been accepted for clearing by a clearing agency that has its principal place of business in the United States or because it has been executed on a platform that has its principal place of business in the United States. See proposed rules 908(a)(ii) and (iii).

unregistered U.S. person.[349] We preliminarily believe that, in such a transaction, the U.S. person or the non-U.S. person engaged in a security-based swap transaction, in connection with its dealing activity, using personnel located in a U.S. branch or office may generally be more likely than its counterparty to have the ability to report the transaction to a registered SDR given that it has operations in the United States. We also note that, in a transaction where neither side includes a registered security-based swap dealer or a registered major security-based swap participant, placing the duty on the side that has a presence in the United States should better enable us to monitor and enforce compliance with the reporting requirement.

Finally, we are proposing a rule that would provide that a registered broker-dealer (including a registered SB SEF) shall report the information required by rules 901(c) and 901(d) for any transaction in which neither side includes a U.S. person and neither side includes a non-U.S. person that falls within proposed rule 908(b)(5) but the security-based swap is effected by or through the registered broker-dealer (including a registered SB SEF).[350] We preliminarily believe that, in such a transaction, the registered broker-dealer (including a registered SB SEF) may generally be more likely than the counterparties to the transaction (neither of which may have any operations or presence in the United States) to have the ability to report the transaction to a registered SDR given its presence in the United States and its familiarity with the Commission's regulatory requirements.[351]

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349 See proposed rule 901(a)(2)(ii)(E)(3).

350 See proposed rule 901(a)(2)(ii)(E)(4).

351 Cf. Letter from ISDA to SEC, dated January 18, 2011 ("ISDA/SIFMA Letter") at 17 (noting that market participants, including brokers, may provide reporting services on behalf of their customers).

6. Proposed amendments to rules 900(u), 901(d)(9), 906(b), 906(c), and 907(a) of Regulation SBSR to accommodate proposed rule 901(a)(2)(ii)(E)(4).

(a) Proposed amendment to rule 900(u)

Rule 900(u) defines a "participant" of a registered SDR as "a counterparty, that meets the criteria of [rule 908(b) of Regulation SBSR], of a security-based swap that is reported to that [registered SDR] to satisfy an obligation under [rule 901(a) of Regulation SBSR]." In the Regulation SBSR Proposed Amendments Release, we proposed to expand the definition of "participant" to include registered clearing agencies and platforms.[352] This proposed definition would not include a registered broker-dealer that incurs reporting obligations solely because it effects a transaction between unregistered non-U.S. persons that do not fall within proposed rule 908(b)(5). We believe that such registered broker-dealers should be participants of any registered SDR to which they are required to report security-based swap transaction information. Imposing participant status on such registered broker-dealers would explicitly require those entities to report security-based swap transaction information to a registered SDR in a format required by that registered SDR under rule 901(h). If such registered broker-dealers were not participants of the registered SDR and were permitted to report data in a format of their own choosing, it could be difficult or impossible for the registered SDR to understand individual transaction reports or aggregate them with other reports in a meaningful way. This could adversely affect the ability of the Commission and other relevant authorities to carry out their oversight responsibilities and could interfere with the ability of a registered SDR to publicly

[352] See Regulation SBSR Adopting Release, 80 FR 14751. As proposed to be amended, rule 900(u) would define "participant" to mean: (1) a person that is a counterparty to a security-based swap, provided that the security-based swap is subject to regulatory reporting under Regulation SBSR and is reported to a registered SDR pursuant to Regulation SBSR; (2) a platform that is required to report a security-based swap pursuant to Rule 901(a)(1); or (3) a registered clearing agency that is required to report a life cycle event pursuant to Rule 901(e).

disseminate security-based swap transaction information as required by rule 902 of Regulation SBSR. Therefore, we are proposing to amend the definition of "participant" in rule 900(u) to include a registered broker-dealer that is required to report a security-based swap by rule 901(a)(2)(ii)(E)(4).

If we ultimately adopt both this amendment to rule 900(u) and the amendment proposed in the Regulation SBSR Proposed Amendments Release, "participant" would mean: "with respect to a registered security-based swap data repository, [] (1) a counterparty, that meets the criteria of § 242.908(b), of a security-based swap that is reported to that registered security-based swap data repository to satisfy an obligation under § 242.901(a); (2) a platform that reports a security-based swap to that registered security-based swap data repository to satisfy an obligation under § 242.901(a); (3) a registered clearing agency that is required to report to that registered security-based swap data repository whether or not it has accepted a security-based swap for clearing pursuant to § 242.901(e)(1)(ii); or (4) a registered broker-dealer (including a registered security-based swap execution facility) that is required to report a security-based swap to that registered security-based swap data repository by § 242.901(a)."

(b) Proposed amendment to rule 901(d)(9)

In the Regulation SBSR Adopting Release, we noted the importance of identifying whether a broker is involved in the execution of a security-based swap. Identifying the broker for a security-based swap will provide regulators with a more complete understanding of the transaction and could provide useful information for market surveillance purposes.[353] To obtain information about brokers that facilitate security-based swap transactions—as well as other persons involved in a security-based swap—existing rule 901(d)(2) requires the reporting side to

[353] See Regulation SBSR Adopting Release, 80 FR 14583.

report, as applicable, the branch ID, broker ID, execution agent ID, trade ID, and trading desk ID of the direct counterparty on the reporting side. In the Regulation SBSR Adopting Release, we also recognized the importance of identifying the venue on which a security-based swap is executed, because this information should enhance the ability of relevant authorities to conduct surveillance in the security-based swap market and understand developments in the security-based swap market generally.[354] Therefore, we adopted rule 901(d)(9), which requires reporting of the platform ID, if applicable.

As described above, proposed rule 901(a)(2)(ii)(E)(4) would require a registered broker-dealer to report the information in rules 901(c) and 901(d) for any transaction between two unregistered non-U.S. persons that do not fall within rule 908(b)(5) where the transaction is effected by or through the registered broker-dealer. Because a security-based swap reported under rule 901(a)(2)(ii)(E)(4) will not have a reporting side, no one would have the obligation to report the information required by existing rule 901(d)(2). We preliminarily believe, however, that being able to identify any registered broker-dealer that effects a security-based swap transaction in the manner described in rule 901(a)(2)(ii)(E)(4) would enhance our understanding of the security-based swap market and would improve our ability, and the ability of other relevant authorities, to conduct surveillance of security-based swap market activities. We therefore propose to amend rule 901(d)(9) to assure that the identity of any such registered broker-dealer is included in the report of a security-based swap transaction reported pursuant to rule 901(a)(2)(ii)(E)(4). As proposed to be amended, rule 901(d)(9) would require reporting of "[t]he platform ID, if applicable, or if a registered broker-dealer (including a registered security-based swap execution facility) is required to report the security based swap by §

[354] See Regulation SBSR Adopting Release, 80 FR 14589.

242.901(a)(2)(ii)(E)(4), the broker ID of that registered broker-dealer (including a registered security-based swap execution facility)."

(c) Proposed amendments to rules 906 and 907

Under the proposed amendment to rule 900(u) described above,[355] the definition of "participant" would be expanded to include a registered broker-dealer that incurs reporting obligations solely because it effects a transaction between two unregistered non-U.S. persons that do not fall within proposed rule 908(b)(5). Rule 906(b) of Regulation SBSR generally requires a participant of a registered SDR to provide the identity of its ultimate parent and any affiliates that also are participants of that registered SDR. In the Regulation SBSR Proposed Amendments Release, we proposed to except platforms and registered clearing agencies from rule 906(b).[356] We preliminarily believe that the purposes of rule 906(b)—namely, facilitating our ability to measure derivatives exposure within the same ownership group—would not be advanced by applying the requirement to a registered broker-dealer that incurs reporting obligations solely because it effects a transaction between two unregistered non-U.S. persons that do not fall within proposed rule 908(b)(5) to report parent and affiliate information to a registered SDR. A registered broker-dealer acting solely as a broker with respect to a security-based swap is not taking a principal position in the security-based swap. To the extent that such a registered broker-dealer has an affiliate that transacts in security-based swaps, such positions could be derived from other transaction reports indicating that affiliate as a counterparty. Accordingly, we propose to amend rule 906(b) to state that reporting obligations under rule 906(b) do not

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355 See Section V.E.6, supra.

356 See Regulation SBSR Adopting Release, 80 FR 14645-46.

apply to a registered broker-dealer that becomes a participant solely as a result of making a report to satisfy an obligation under rule 901(a)(2)(ii)(E)(4).

We propose to make a similar amendment to rule 907(a)(6). In the Regulation SBSR Proposed Amendments Release, we proposed to amend this rule to require a registered SDR to have policies and "[f]or periodically obtaining from each participant other than a platform or a registered clearing agency information that identifies the participant's ultimate parent(s) and any participant(s) with which the participant is affiliated, using ultimate parent IDs and counterparty IDs."[357] We now propose to further amend rule 907(a)(6) and except from this requirement a registered broker-dealer that incurs reporting obligations solely because it effects a transaction between two unregistered non-U.S. persons that do not fall within proposed rule 908(b)(5). Thus, if we ultimately adopt both this amendment to rule 907(a)(6) and the amendment to rule 907(a)(6) proposed in the Regulation SBSR Proposed Amendments Release, rule 907(a)(6) would require a registered SDR to have policies and procedures "[f]or periodically obtaining from each participant other than a platform, a registered clearing agency, or a registered broker-dealer (including a registered security-based swap execution facility) that becomes a participant solely as a result of making a report to satisfy an obligation under § 242.901(a)(2)(ii)(E)(4) information that identifies the participant's ultimate parent(s) and any participant(s) with which the participant is affiliated, using ultimate parent IDs and counterparty IDs."

(d) Extending the applicability of rule 906(c)

Rule 906(c) requires certain participants of a registered SDR to establish, maintain, and enforce written policies and procedures that are reasonably designed to ensure that the

[357] Once a participant reports parent and affiliate information to a registered SDR, rule 906(b) requires the participant to "promptly notify the registered [SDR] of any changes" to its parent and affiliate information.

participant complies with any obligations to report information to a registered SDR in a manner consistent with Regulation SBSR. Rule 906(c) also requires participants covered by the rule to review and update their policies and procedures at least annually. In the Regulation SBSR Adopting Release, we stated that the policies and procedures required by rule 906(c) are intended to promote complete and accurate reporting of security-based swap information by SDR participants that are registered security-based swap dealers or registered major security-based swap participants.[358]

In the Regulation SBSR Proposed Amendments Release, we proposed to amend rule 906(c) by extending the requirement to have such policies and procedures to platforms and registered clearing agencies.[359] In light of the proposed amendments to rule 901(a) relating to registered broker-dealers, described above, we now preliminarily believe that a registered broker-dealer that incurs reporting obligations solely because it effects transactions between two unregistered non-U.S. persons that do not fall within proposed rule 908(b)(5) also should be required to establish, maintain, and enforce the policies and procedures required by rule 906(c).[360]

We preliminarily believe that the proposed amendment to rule 906(c) should result in greater accuracy and completeness of the security-based swap transaction data reported to registered SDRs. Without written policies and procedures, compliance with reporting

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358 See Regulation SBSR Adopting Release, 80 FR 14648.

359 See id. at 14758-59.

360 We are also proposing to revise the title of the rule. As adopted, the title of rule 906(c) was: "Policies and procedures of registered security-based swap dealers and registered major security-based swap participants." In the Regulation SBSR Proposed Amendments Release, we proposed to add registered clearing agencies and platforms to the rule's title. Rather than adding registered broker-dealers to the entities delineated in the title to 906(c), we are proposing to revise the title to "Policies and procedures to support reporting compliance."

obligations of such a registered broker-dealer might depend too heavily on key individuals or unreliable processes. For example, if knowledge of the reporting function was not reflected in written policies and procedures but existed solely in the memories of one or a few individuals, compliance with applicable reporting requirements by the firm might suffer if these key individuals depart the firm. We preliminarily believe, therefore, that requiring participants that are registered broker-dealers that incur reporting obligations solely because they effect a transaction between two non-U.S. persons that do not fall within proposed rule 908(b)(5) to establish, maintain, and enforce written policies and procedures should promote clear, reliable reporting that can continue independent of any specific individuals. We further believe that requiring such a participant to establish, maintain, and enforce written policies and procedures relevant to its reporting responsibilities, as would be required by the proposed amendment to rule 906(c), would help to improve the degree and quality of overall compliance with the reporting requirements of Regulation SBSR.

7. Availability of substituted compliance

Rule 908(c)(1) of Regulation SBSR describes the security-based swap transactions that potentially would be eligible for substituted compliance with respect to regulatory reporting and public dissemination of security-based swap transactions. Accordingly, substituted compliance would potentially be available for transactions that would become subject to Regulation SBSR pursuant to the proposed amendments described above, as the location of relevant dealing activity or of execution of the transaction would continue to be irrelevant for purposes of rule 908(c).[361]

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[361] See note 295, supra.

Rule 908(c)(1) does not condition substituted compliance eligibility on where a particular transaction was arranged, negotiated, or executed.[362] Under rule 908(c)(1), a security-based swap is eligible for substituted compliance with respect to regulatory reporting and public dissemination, provided that at least one of the direct counterparties to the security-based swap is either a non-U.S. person or a foreign branch. Thus, rule 908(c)(1) permits a security-based swap between a U.S. person and the New York branch of a foreign bank (i.e., a non-U.S. person with operations inside the United States) to be eligible for substituted compliance, provided that such compliance is with the rules of a foreign jurisdiction that is the subject of a Commission substituted compliance order.

In adopting rule 908(c)(1), we noted that the final rule was consistent with our decision to solicit additional comments regarding whether to impose reporting or public dissemination requirements based solely on whether a transaction is conducted within the United States.[363] Although we are now proposing an amendment that would impose these requirements on certain transactions that a non-U.S. person arranges, negotiates, or executes using personnel located in a U.S. branch or office, we are not proposing an amendment that would limit the availability of substituted compliance for such transactions based on the location of this relevant activity. Accordingly, under our proposed approach, and consistent with our final rule, counterparties to a transaction that is required to be reported because a non-U.S.-person counterparty to the transaction, in connection with its dealing activity, arranged, negotiated, or executed the

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362 Rule 908(c)(1) provides: "Compliance with the regulatory reporting and public dissemination requirements in sections 13(m) and 13A of the Act (15 U.S.C. 78m(m) and 78m-1), and the rules and regulations thereunder, may be satisfied by compliance with the rules of a foreign jurisdiction that is the subject of a Commission order described in paragraph (c)(2) of this section, provided that at least one of the direct counterparties to the security-based swap is either a non-U.S. person or a foreign branch."

363 See Regulation SBSR Adopting Release, 80 FR 14658.

transaction using personnel located in a U.S. branch or office or because it was executed on a platform or effected by or through a registered broker-dealer would be eligible for substituted compliance, provided that such compliance is with the rules of a foreign jurisdiction that is the subject of a Commission order.[364]

This approach would subject transactions that are arranged, negotiated, or executed by personnel located in a U.S. branch or office, in connection with a non-U.S. person's dealing activity, to regulatory reporting and public dissemination requirements in a manner consistent with Title VII, while mitigating the potential to duplicate compliance burdens. The proposed approach is also consistent with the determination in our final rule that certain transactions involving U.S.-person counterparties are eligible for substituted compliance (i.e., when the transaction is through the foreign branch of the U.S. person) even if the non-U.S.-person counterparty has engaged in dealing activity in connection with the transaction in the United States.[365]

F. Request for Comment

We invite comment regarding all aspects of the proposed approach to clearing, trade execution, regulatory reporting, and public dissemination described here, as well as potential alternative approaches. Data and comment from market participants and other interested parties regarding the likely effect of the proposed approach and of potential alternative approaches will be particularly useful to us in evaluating potential modifications to the re-proposal.

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[364] A non-U.S. person engaged in relevant dealing activity using personnel located in a U.S. branch or office may incur the duty to report a transaction under Exchange Act rules 901(a)(2)(ii)(A), (B), (C), or (D), or under proposed rules 901(a)(2)(ii)(E)(2), (3), or (4) of Regulation SBSR.

[365] See Exchange Act rule 908(c)(1) (permitting compliance with the regulatory reporting and public dissemination requirements by complying with the rules of a foreign jurisdiction if at least one of the direct counterparties to the security-based swap transaction is either a non-U.S. person or a foreign branch).

In addition, we specifically request comment with respect to each of the requirements discussed above, as follows.

1. Mandatory clearing and trade execution

We seek comment on the re-proposed rule regarding application of mandatory clearing and trade execution in all aspects, including the following:

- Is it appropriate not to apply the clearing and trade execution requirements to transactions that a non-U.S. person, in connection with its dealing activity, arranges, negotiates, or executes using personnel located in a U.S. branch or office? Why or why not?
- What would be the likely market impact of our proposal not to subject such transactions to the clearing and trade execution requirements? How would this proposed approach affect the competitiveness of U.S. persons and other market participants in the global marketplace (both in the United States as well as in foreign jurisdictions)? How do you believe any competitive disparity that may result under our proposed approach should be addressed by our rules?
- Would there be any potential effect from our proposal on U.S. financial stability? If so, how should any such effect be addressed?
- Would there be any potential effect from our proposal on the liquidity available on any SB SEFs? If so, how should any such effect be addressed?
- To what extent do non-U.S. persons that are not engaged in security-based swap dealing but do enter into security-based swaps with dealers that use personnel located in the United States already have clearing relationships with clearing agencies located in the United States or with entities that may qualify for a

substituted compliance determination? For such persons that do not already have such relationships, what costs and other burdens would be involved with establishing such relationships? To what extent would permitting substituted compliance as proposed in the Cross-Border Proposing Release address these concerns?

2. Regulation SBSR

We request comment on all aspects of the proposed amendments to Regulation SBSR, including the following:

- Do you agree with the approach taken in the proposed amendments to rule 908(a) that a security-based swap should be subject to regulatory reporting and public dissemination regardless of the nationality or place of domicile of the counterparties if it is a transaction connected with a person's security-based swap dealing activity that is arranged, negotiated, or executed by personnel located in the United States? Why or why not?
- Do you agree with the approach taken in the proposed amendments to rule 908(a) that a security-based swap executed on a platform having its principal place of business in the United States should be subject to the regulatory reporting and public dissemination requirements? Why or why not?
- Do you agree with the approach taken in the proposed amendments to rule 908(a) that would subject a security-based swap effected by or through a registered broker-dealer (including a registered security-based swap execution facility) to the regulatory reporting and public dissemination requirements? Why or why not? Should transactions that would be required to be reported under the

proposed amendments to rule 908(a) solely because they were effected by or through a registered broker-dealer (including a registered security-based swap execution facility) be required to be reported by a counterparty to the transaction, rather than by a registered broker-dealer (including a registered security-based swap execution facility), as proposed?

- Do you agree with the proposed amendment to the hierarchy of reporting obligations in rule 901(a)? Why or why not? Are there any prongs where you believe the result should be different? If so, which prong(s) and why?
- Should we provide an exemption from Regulation SBSR's public dissemination requirement for transactions having a U.S. person guarantor in which the other side includes no counterparty (direct or indirect) that is a U.S. person, registered security-based swap dealer, or registered major security-based swap participant? Why or why not?
- What types of controls would be necessary to identify transactions required to be reported under rule 908(a)(1)(v)? How would this work as an operational matter? What are the costs and benefits associated with developing and maintaining such controls?
- As noted above, given the limitation on reporting duties set forth in rule 908(b) and in the proposed amendments to that rule, we expect that most, if not all, registered broker-dealers required to report under this proposed amendment would be U.S. persons intermediating security-based swap transactions between non-U.S. person counterparties and that such persons would be effecting transactions in security-based swaps from their offices in the United States. Is

this expectation consistent with market practices by registered broker-dealers?

- Should a registered broker-dealer that is required to report transactions pursuant to rule 901(a)(2)(ii)(E)(4) be a participant of the registered SDRs to which they report? If not, how would a registered SDR ensure that such persons provide data in a format required by the registered SDR? Would a registered broker-dealer likely be required to be a participant of a registered SDR under existing rule 901(d) by virtue of its other security-based swap activity?
- Do you agree that the Commission should require reporting of the identity of any registered broker-dealer that effects a security-based swap for two non-U.S. person that do not fall within rule 908(b)(5)? Why or why not? If so, do you believe that the proposed amendment to rule 901(d)(9) is the appropriate way to accomplish that goal? Why or why not?
- Do you agree with the Commission's proposal to exclude registered broker-dealers that incur reporting obligations solely because they effect a transaction between two non-U.S. persons that do not fall within proposed rule 908(b)(5) from rule 906(b)? Why or why not?
- Do you believe that rule 906(c) should be expanded to include registered broker-dealers that incur reporting obligations solely because they effect a transaction between two non-U.S. persons that do not fall within proposed rule 908(b)(5)? Why or why not?
- What would be the costs to registered broker-dealers that would be subject to rule 901(a)(2)(ii)(E)(4) for establishing and maintaining policies and procedures under rule 906(c) to support compliance with Regulation SBSR? Are these registered

broker-dealers likely to have affiliates that will become registered security-based swap dealers, which are already subject to rule 906(c)? If so, would these registered broker-dealers be able to reduce implementation burdens under rule 906(c) by adapting the policies and procedures of their affiliates for their own usage?

VI. Economic Analysis of the Proposed Rules

The proposed amendments and proposed rule would determine when a non-U.S. person whose obligations under a security-based swap are not guaranteed by a U.S. person and that is not a conduit affiliate is required to include in its dealer de minimis calculation transactions with another non-U.S. person and when transactions of a non-U.S. person whose obligations under a security-based swap are not guaranteed by a U.S. person are subject to the external business conduct requirements and to Regulation SBSR.

We are sensitive to the economic consequences and effects, including costs and benefits, of our rules. The following economic analysis identifies and considers the costs and benefits—including the effects on efficiency, competition, and capital formation—that may result from the rules being proposed today. These costs and benefits are discussed below and have informed the policy choices described throughout this release. Because of the attributes of the security-based swap market, the market's global nature, the concentration of dealing activity, and the ease with which dealers can relocate their operations to different jurisdictions, we preliminarily believe that the territorial approach to transactions proposed in these rules is consistent with the statutory focus of the Title VII framework for security-based swaps. Below, we discuss the likely economic effects of the proposed rules, including the assessment and programmatic costs and benefits. We also discuss the potential economic effects of certain alternatives to the approach taken by the proposed rules.

A. Assessment Costs

1. Discussion

Under the proposed rules we preliminarily believe that non-U.S. persons would incur costs to assess whether their activities must be counted against de minimis thresholds and subjected to Title VII requirements.[366] This section begins by considering the effect on assessment costs of increasing the scope of transactions required to be counted towards de minimis thresholds and proceeds to consider the effect on assessment costs of identifying security-based swap activity that, under the proposed rules, would count towards de minimis thresholds or become subject to external business conduct, regulatory reporting, and public dissemination requirements.

Because the proposed amendment would expand the scope of security-based swap transactions that non-U.S. persons would need to include in their de minimis calculations, we preliminarily believe that the proposed amendment may result in an increase in the number of non-U.S. persons exceeding $2 billion in transaction notional in a given year and incurring assessment costs as a result of counting transactions against the de minimis threshold.[367]

Estimating the number of additional non-U.S. persons that we expect to incur assessment costs as a result of the proposed amendment would require adding transactions arranged, negotiated, or executed by personnel located in the United States, including cleared anonymous

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366 We refer to these costs as "Assessment Costs." See Intermediary Definitions Adopting Release, 77 FR 30722.

367 We preliminarily believe that it is likely that entities that exceed $2 billion in transaction notional in a 12 month period are likely to incur assessment costs to determine whether they exceed the de minimis threshold. Because the proposed rules add to the set of transactions that must be counted towards the de minimis threshold, non-U.S. persons are more likely to exceed $2 billion in transaction notional and incur these assessment costs. These non-U.S. persons would have to assess not only transactions scoped in by the proposed rule, but also transactions with U.S. persons against their de minimis threshold. See Cross-Border Adopting Release, 79 FR 47331-33.

transactions subject to proposed rule 3a71-5(c), to the set of transactions that these non-U.S. persons are currently required to count as a result of rule 3a71-3(b)(1)(iii) and computing the total notional value of these transactions. We cannot determine, based on the TIW transactions data, whether particular transactions were arranged, negotiated, or executed by personnel located in the United States. If we assume that all observable transactions of non-U.S. persons on U.S. reference entities that are not already required to be applied towards the de minimis threshold as a result of proposed rule 3a71-3(b)(1)(iii) are arranged, negotiated, or executed by personnel located in a U.S. branch or office, we estimate that a total of approximately 15 non-U.S. persons likely would incur assessment costs as a result of the proposed amendment based on 2014 TIW transactions data. However, we note that this estimate may be overinclusive, as we do not believe that all such transactions are likely to be arranged, negotiated, or executed by personnel located in a U.S. branch or office, and at the same time it may also be underinclusive because our TIW data does not include single-name CDS transactions between two non-U.S. entities written on non-U.S. underliers.[368]

The additional 15 non-U.S. persons that are likely to incur assessment costs associated with de minimis counting would join the 56 non-U.S. persons identified in the TIW 2014 transactions data as having relevant activity under rule 3a-71-3(b),[369] for a total of 71 persons who would likely incur assessment costs under the proposed rules based on 2014 data. We preliminarily believe it is reasonable to increase these estimates by a factor of two, to account for any potential growth in the security-based swap market and to account for the fact that we are limited to observing transaction records for activity between non-U.S. persons that reference

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368 We note that TIW's definitions of U.S. and non-U.S. entities do not necessarily correspond to the definition of U.S. person under Rule 3a71-3(a)(4).

369 See Section II.B.1(c).

U.S. underliers.[370] As a result, we preliminarily believe that the assessment costs discussed below apply to 142 entities.

Although foreign security-based swap dealers that are required to register under existing Exchange Act rule 3a71-3 would not be likely to incur assessment costs as a result of 3a71-3(b)(1)(iii), as this proposed rule would not affect their need to register as security-based swap dealers, they are included in our total estimate of 142 entities above. We have included them because they likely would incur identical assessment costs in order to identify transactions subject to those requirements under proposed Exchange Act rule 3a71-5(c), which imposes external business conduct requirements on the U.S. business of registered security-based swap dealers, and the proposed amendments to Regulation SBSR.

As noted above, we preliminarily believe that, as a result of the proposed rules, non-U.S. persons would incur costs to identify transaction activity that is relevant for de minimis counting and subject to external business conduct, regulatory reporting, and public dissemination requirements. We preliminarily believe that the business structures employed by non-U.S. persons may determine the magnitude of these assessment costs, and that non-U.S. persons will generally choose a business structure that considers its regulatory costs for both compliance and assessment. The following section discusses the approaches that these market participants may use to determine which transactions are subject to Title VII regulation under our proposed approach and, to the extent possible, presents estimates of assessment costs on a per-entity basis.

First, non-U.S. persons may perform assessments on a per-transaction basis, which some commenters have suggested could lead market participants to incur significant costs.[371] We

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[370] See Intermediary Definitions Adopting Release, 77 FR 30725 n.1457.

recognize that performing these assessments could involve one-time costs associated with developing computer systems to capture information about the location of personnel involved with each transaction in addition to ongoing costs of analyzing these data and modifying classification of transaction activity as personnel or offices change locations over time. However, we preliminarily believe that the approach we are proposing in this release should considerably mitigate these costs. This proposed approach should be considerably easier than the initially proposed approach for market participants to integrate into existing transaction monitoring systems or order management systems given its focus on market-facing activity of personnel of the entity (or personnel of the agent of the entity) engaged in dealing activity that is located in the United States.

Accordingly, based on staff understanding regarding the development and modification of information technology (IT) systems that track the location of firm inputs, we preliminarily estimate the start-up costs associated with developing and modifying these systems to track the location of persons with dealing activity will be $410,000 for the average non-U.S. entity. To the extent that non-U.S. persons already employ such systems, the costs of modifying such IT systems may be lower than our estimate.

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[371] See note 289, supra (citing ISDA Letter); note 108, supra (citing SIFMA/FIA/FSR Letter); note 109, supra (citing AFR Letter); notes 110 and 112, supra (citing IIB Letter). Other commenters noted the additional cost burden that market participants would face if the definition diverged from that of the CFTC. See note 111 (citing SIFMA/FIA/FSR Letter, Pensions Europe Letter, IIB Letter, and JFMC Letter). Comments on the CFTC Cross-Border Guidance also identified the issue of costs associated with an activity-based approach. See notes 131 and 133-134, supra (citing letters raising this concern).

In addition to the development or modification of IT systems, we preliminarily believe that entities would incur the cost of $6500 per year on an ongoing basis for training, compliance, and verification costs.[372]

Second, non-U.S. firms might additionally restrict personnel located in the United States from arranging, negotiating, or executing security-based swaps in connection with the non-U.S. firm's dealing activity with non-U.S.-person counterparties. Such restrictions on communication and staffing for the purposes of avoiding certain Title VII requirements would reduce the costs of assessing the territorial status of each trade, and may entirely remove the need for a system that assesses the location of personnel on a trade-by-trade basis. However, this reduction in assessment costs may be offset by the additional costs of duplicating personnel in foreign and U.S. locations.

While we do not currently have data necessary to precisely estimate these costs in total, we can estimate the costs of establishing policies and procedures to restrict communication between personnel located in the United States employed by non-U.S. persons (or their agents,) and other personnel involved in dealing activity. Based on staff experience, we preliminarily estimate that establishing policies would take a non-U.S. person approximately 100 hours and would cost approximately $28,300 for each entity that chooses this approach.[373] Further, we

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372 Calculated as Internal Cost, 90 hours x $50 per hour = $4,500 plus Consulting Costs, 10 hours x $200 per hour = $2,000, for a total cost of $6,500.

373 Calculated as Compliance Manager, 100 hours x $283 per hour = $28,300. We use salary figures from SIFMA's Management & Professional Earnings in the Securities Industry 2013, modified by SEC staff to account for an 1,800-hour work-week and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

The costs of policies and procedures are based on burden estimates in the recent Nationally Recognized Statistical Rating Organizations; Final Rule, Exchange Act Release No. 72936 (August 27, 2014), 79 FR 55078 (September 15, 2015) ("NRSRO Adopting Release"). Specifically, we assume that the policies and procedures required to restrict communication between U.S. and non-U.S. personnel are similar to policies and procedures required to eliminate

preliminarily believe that the total costs incurred by entities that choose to restrict communication between personnel would be determined by the number of entities that choose such an approach as well as the number of additional personnel that these entities must hire as a result of restricted communication.

We preliminarily believe that non-U.S. persons that primarily trade with non-U.S. persons on non-U.S. reference entities may be most likely to undertake this approach. However, because our access to TIW transactions data is limited to transactions in which at least one counterparty is U.S.-domiciled or the reference entity is a U.S. entity, we cannot at this time estimate the size of this set of participants.

Third, a dealer may choose to comply with applicable Title VII requirements, regardless of whether they in fact apply, to avoid assessing the locations of personnel involved with each transaction. This strategy may be preferred by a non-U.S. person engaged in dealing activity that expects few transactions involving other non-U.S. persons to be arranged, negotiated, and executed by personnel located outside the United States, such as a non-U.S. person that primarily trades in U.S. reference entities and generally relies on personnel located in the United States to perform market-facing activities. For these participants, the savings from not following policies and procedures developed for Title VII compliance purposes for the few transactions that do not involve dealing activity by personnel from a location in the United States might be less costly than the costs of implementing a system to track the locations of personnel on a trade-by-trade basis. Similarly, registered foreign security-based swap dealers may also prefer this approach, as they would only be required to comply with Title VII external business conduct requirements,

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conflicts of interest under Rule 17g-5(c)(8). See NRSRO Adopting Release, 79 FR 55239, 55249.

and their security-based swap transactions, which would already be required to be reported under Regulation SBSR, also would be publicly disseminated.

We preliminarily believe that the same principles apply to non-U.S. persons that rely on agents to arrange, negotiate, or execute security-based swaps on their behalf. We anticipate that these agents of non-U.S. persons may employ any of the strategies above to comply with the proposed rules. Non-U.S. persons may rely on representations from their agents about whether transactions conducted on its behalf contained dealing activity by personnel from a location in the United States. This may occur on a transaction-by-transaction basis, or, if the agent complies with Title VII requirements by default, via a representation about the entirety of the agent's business.

We preliminarily believe that all the methods described above are likely to involve an initial one-time review of security-based swap business lines to help each entity determine which of the business structures outlined above is optimal. This review would encompass both employees of potential registrants as well as employees of agents used by potential registrants and would identify whether these personnel are involved in arranging, negotiating, or executing security-based swaps. The information gathered as a result of this review would allow a foreign security-based swap dealer to assess the revenues it expects to flow from transaction activity performed by personnel located in the United States. This information would also help these market participants form preliminary estimates about the costs associated with various alternative structures, including the trade-by-trade analysis outlined below. This initial review may be followed with reassessment at regular intervals or subsequent to major changes in the market participant's security-based swap business, such as acquisition or divestiture of business units. We preliminarily believe that this type of review of business lines would be similar in

nature to the analysis needed to produce financial statements for a large financial institution. However, we acknowledge that evaluating alternative structures to determine costs associated with assessment and compliance may require additional legal analysis. We preliminarily estimate that the per-entity initial costs of a review of business lines would be approximately $102,000.[374] Further, we preliminarily believe that periodic reassessment of business lines would cost, on average, $52,000 per year, per entity.[375]

Additionally, we preliminarily believe that our proposed approach may impose certain costs on U.S. security-based swap dealers conducting business through a foreign branch, and registered broker-dealers (including registered SB SEFs) that intermediate trade in the security-based swap market. First, under the proposed approach, U.S. security-based swap dealers conducting business through a foreign branch will also need to classify their counterparties and transactions in order to determine what activity constitutes their foreign business. Based on analysis of 2014 TIW transactions data, we continue to estimate that no more than five security-based swap dealers will conduct dealing activity through foreign branches. Assuming that all such entities elect to establish a system to identify their foreign business, we preliminarily estimate the total assessment costs associated with the proposed approach to be approximately $75,000, with ongoing, annual costs of approximately $84,000.[376]

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374 Calculated as (Senior Accountant, 500 hours x $198 per hour) + (Compliance Attorney, 2 hours x $334 per hour) + (Compliance Manager, 8 hours x $283 per hour) = $101,932.

375 Calculated as (Senior Accountant, 250 hours x $198 per hour) + (Compliance Attorney, 4 hours x $334 per hour) + (Compliance Manager, 4 hours x $283 per hour) = $51,968. We use salary figures from SIFMA's Management & Professional Earnings in the Securities Industry 2013, modified by SEC staff to account for a 1,800-hour work-week and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

376 These figures correspond to estimates provided initially in the Cross-Border Proposing Release and updated in the Cross-Border Adopting Release. See Cross-Border Proposing Release, 78 FR 31153. See also Cross-Border Adopting Release, 79 FR 47332.

Second, registered broker-dealers (including registered SB SEFs) may incur assessment costs in connection with proposed rule 901(a)(2)(ii)(E)(4). Under the proposed rule, these entities would be required to report security-based swap transactions that they intermediate if neither side includes a U.S. person; a registered security-based swap dealer or major security-based swap participant; or a non-U.S. person that arranged, negotiated, or executed the security-based swap using its personnel, or using personnel of its agent, in a U.S. branch or office. As a result, we preliminarily believe that these entities would be required to assess the nature of transactions they intermediate.

We preliminarily believe that assessment by registered broker-dealers (including registered SB SEFs) would require an analysis of their clients (in the case of registered-broker dealers that are not registered SB SEFs) and members (in the case of registered SB SEFs). We preliminarily believe that registered broker-dealers and SB SEFs are likely to collect information about the counterparties they serve and maintain these records as part of their existing business. On the basis of these existing data, registered broker-dealers and SB SEFs would be able to determine the U.S. person status, registration status, and the location of personnel of their clients and members (or the personnel of agents of their clients and members) that submit orders.

Further, we preliminarily believe that registered broker-dealers and SB SEFs may be able to determine, on the basis of their own business models or on the basis of activity they support, whether their unregistered non-U.S. clients' and members' transactions are a result of dealing activity, and so would be able to identify which transactions of unregistered non-U.S. persons would need to be reported. For example, a registered broker-dealer that operates as an interdealer broker can likely expect that unregistered non-U.S. person clients are engaging in dealing activity.

As a result, we preliminarily believe that the assessment costs incurred by registered broker-dealer (including registered SB SEFs) are likely limited to an analysis of clients and members to identify the subset of clients and members whose trades they are obligated to report under the proposed rules, supported by systems that would record and maintain this information over time. We preliminarily believe that these costs are similar in nature to legal costs related to systems and analysis, as well as the direct costs of systems and analysis, discussed in the Cross-Border Proposing Release. We estimate that, as a result of the proposed rules imposing reporting obligations on registered broker-dealers (including SB SEFs), each of these entities would incur upfront costs of $45,304,[377] and ongoing costs of $16,612 per year.[378] We note that registered broker-dealers and SB SEFs may, like counterparties, choose alternative business structures to mitigate these costs, as discussed above. For example, they may offer transaction reporting services to their clients for a fee and report all transactions they intermediate, thus precluding the need to assess their clients' and members' activity.

Finally, we preliminarily believe that this proposed approach mitigates the concerns of some commenters regarding the costs associated with the use of the defined term "transactions conducted within the United States" as originally proposed in the Cross-Border Proposing Release.[379] In particular, by focusing on dealing activity, the proposed approach should

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377 This estimate is calculated as the sum of (Attorney at $380 per hour x 80 hours) = $30,400, and the upfront costs of systems as calculated in the Cross-Border Adopting Release. See Cross-Border Adopting Release, 79 FR 47332. We use salary figures from SIFMA's Management & Professional Earnings in the Securities Industry 2013, modified by SEC staff to account for an 1800-hour work-week and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

378 See Cross-Border Adopting Release, 79 FR 47332.

379 See, e.g., Section III.B.2(c), supra (discussing letters raising cost concerns about initially proposed approach).

eliminate the need for non-U.S. persons that do not engage in dealing activity to assess whether they or their counterparties engage in relevant activity in the United States.[380]

2. Request for comment

We request comment on all aspects of the re-proposed rule regarding its economic analysis of the application of the de minimis exception to non-U.S. persons arranging, negotiating, or executing security-based swaps using personnel located in the United States, as well as the application of external business conduct requirements for registered security-based swap dealers, associated with such transactions, including the following:

- We have preliminarily estimated assessment costs associated with determining whether transaction activity is arranged, negotiated, or executed using personnel, or the personnel of agents, located in a U.S. branch or office on a transaction-by-transaction basis, by identifying market-facing personnel involved in each transaction. Are these estimates reasonable with respect to both the use of a non-U.S. person's personnel and of its agent's personnel? Please provide data that would assist us in making more accurate estimates of these assessment costs.
- We have preliminarily suggested that some non-U.S. persons might comply with Title VII by default to reduce assessment costs. Is this suggestion reasonable? Please provide data that would assist us in making more accurate estimates of the assessment costs in these situations.
- We have preliminarily suggested that non-U.S. market participants would review business lines to determine which compliance and assessment program is optimal. Are non-U.S. market participants likely to carry out such reviews under the

[380] See, e.g., note 104, supra (citing MFA/AIMA Letter).

proposed rules? Please provide data that would assist us in computing estimates of the costs of these reviews on an ongoing basis.

- Are there alternative methods that market participants may use to comply with the proposed rules other than those described above? If so, please describe the method and the costs of such method.
- Under the proposed rules, registered brokers-dealers (including registered SB SEFs) would be required to report certain transactions to a registered SDR. Please provide any additional information or data that would assist us in estimating the assessment costs such registered broker-dealers (including registered SB SEFs) may incur in determining their obligation to report.
- We have preliminarily suggested that registered broker-dealers (including registered SB SEFs) would require an analysis of their clients (in the case of registered broker-dealers) and members (in the case of registered SB SEFs), for purposes of reporting transactions pursuant to proposed rule 901(a)(2)(ii)(E)(4). We stated that we preliminarily believe that registered broker-dealers and SB SEFs are likely to collect information about the counterparties they serve and maintain these records as part of their existing business and that registered broker-dealers and SB SEFs would be able to determine the U.S.-person status, registration status, and the location of personnel of their clients and members (or the personnel of agents of their clients and members) that submit orders. Please provide comments as to whether registered broker-dealers and SB SEFs will be able to determine the U.S.-person status, registration status, and location of

personnel of their clients and members (or the personnel of agents of their clients and members) that submit orders. Please explain why or why not.

- We have stated that we preliminarily believe that registered broker-dealers and SB SEFs may be able to determine, on the basis of their own business models or on the basis of activity they support, whether their unregistered non-U.S. clients' and members' transactions are a result of dealing activity, enabling them to identify which transactions of unregistered non-U.S. persons are connected with that non-U.S. person's dealing activity and should be reported. Please provide comments as to whether registered broker-dealers and SB SEFs may be able to make this determination. Please explain why or why not.

B. Programmatic Costs and Benefits

Programmatic costs and benefits arise from applying substantive regulation to those transactions and entities that fall within the scope of the Title VII regulatory regime.[381] In the following sections, we discuss the costs and benefits of each of the Title VII requirements that the proposed rule would apply to transactions with dealing activity by personnel from a location in the United States.

1. De minimis exception

Under our proposed amendment, a non-U.S. person that, in connection with its dealing activity, enters into a transaction with another non-U.S. person would be required to include the transaction in its de minimis calculation if it arranges, negotiates, or executes the transaction using personnel located in a U.S. branch or office. This requirement would also apply to cleared anonymous transactions that are currently exempt from application of the de minimis thresholds

[381] See Intermediary Definitions Adopting Release, 77 FR 30722.

under rule 3a71-5. We are proposing rules that require the dealing counterparty to look only at the location of dealing activity of its own personnel or of its agent's personnel rather than require the dealer to look at the location of both its own activity and that of its counterparty in connection with the transaction, as was originally proposed.[382] This approach is designed to address concerns expressed by some commenters that they would, under the test proposed in the Cross-Border Proposing Release, need to track, on a trade-by-trade basis, where their counterparties are carrying out activities with respect to each transaction.[383]

Because the set of market participants that are subject to dealer regulation, including entity-level requirements under Title VII, will determine the allocation and flow of programmatic costs and benefits arising from these Title VII requirements, the inclusion of these transactions would affect the ultimate costs and benefits of our transaction-level and entity-level rules. At this time, we are unable to precisely estimate the number of potential new dealers that would be required to register because we cannot observe in the data the location of entities' dealing activity. If we assume that all security-based swap dealing activity takes place in the United States, then we currently estimate that no additional entities would be required to register as a result of this proposed rule.[384] However, we believe it is important to acknowledge the potential for additional registrants as a result of the proposed rules as the market evolves.

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382 See initially proposed Exchange Act rules 3a71-3(b)(1)(ii) and 3a71-3(a)(5); Cross-Border Proposing Release, 78 FR 30999.

383 See note 110, supra.

384 In Section VI.A.1, supra, we estimate that 15 entities would exceeded the $2 billion threshold in 2014 as a result of this rule and thus would assess their transactions to determine whether they are required to register as a dealer. Of these 15 entities, we preliminarily believe that none would exceed the $3 billion dealer de minimis threshold and thus be required to register as security-based swap dealers.

If these proposed rules regarding the de minimis exception result in an increased number of non-U.S. persons that eventually register as security-based swap dealers, a larger number of dealers would become subject to requirements applicable to registered dealers under Title VII, including, among others, capital requirements, recordkeeping requirements, and designation of a chief compliance officer. Additionally, an increase in the number of registered dealers would also mean that external business conduct requirements and Regulation SBSR also apply to larger number of transactions, as well as a larger notional volume of transactions.[385] If the proposed rules and amendments result in an increased volume of transaction activity carried out by registered security-based swap dealers, then U.S. financial markets should benefit from more consistent application of Title VII rules designed to mitigate the risk of financial contagion and enhance transparency and counterparty protections, as addressed by regulatory reporting and external business conduct requirements. Our proposed approach to determining which transactions are counted toward a non-U.S. person's de minimis threshold would also bring persons engaged in significant levels of dealing activity using personnel located in in the United States within the Title VII regulatory framework.

Furthermore, status as a security-based swap dealer brings with it specific responsibilities that are categorized as programmatic costs with respect to certain other Title VII requirements.

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[385] Under rule 901(a)(2)(ii), all transactions that include a registered security-based swap dealer on a transaction side are subject to regulatory reporting requirements. We note that our conclusion that the proposed approach will result in these requirements being applied to a larger number of transaction and notional volume of transactions requires the assumption that the demand for liquidity from security-based dealers is not very sensitive to price. Put another way, so long as market participants' demand for risk sharing opportunities provided by security-based swap transactions is relatively inelastic, any reduction in transaction volume due to the costs of Title VII regulation is unlikely to fully offset the increase in the scope of security-based swap transactions subject to Title VII regulation under the proposed rules. If, on the other hand, demand for liquidity is elastic, then the effects of higher costs may dominate any increase in the scope of external business conduct and regulatory reporting requirements, resulting in these requirements applied to a smaller number and lower notional value of transactions.

For example, Regulation SBSR places registered security-based swap dealers at the top of the reporting hierarchy for uncleared transactions.[386] Within this hierarchy, if a registered dealer transacts with an unregistered person, the registered dealer is obligated to report.[387] Thus, as a result of being classified as a dealer, a market participant that may have previously negotiated to place regulatory reporting responsibilities on its counterparties might incur the obligation to report instead.

Finally, certain elements of the Title VII regulatory regime may apply to the existing business of entities that are regulated as security-based swap dealers because they apply not only to transaction activity that cause an entity to meet the definition of a security-based swap dealer, but also to other transaction activity in which the entity participates. Entities that are required to register as security-based swap dealers under rule 3a71-3(b) incur, for example, not only the programmatic costs of external business conduct requirements for their transactions arranged, negotiated, or executed by personnel located in the United States in connection with their dealing activity, but would also be required to comply with external business conduct requirements with respect to all transactions that would be "U.S. business" under the proposed rules. As a result, they may need to develop systems or personnel, such as the designation of a chief compliance officer or the development of recordkeeping and reporting systems, for compliance purposes with respect to their U.S. business.

2. External business conduct requirements

Registered security-based swap dealers must comply with external business conduct requirements. Proposed rule 3a71-3(c) would limit application of these external business

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386 See Exchange Act rule 901(a)(2)(ii)(A); Regulation SBSR Adopting Release, 80 FR 14596.

387 See Exchange Act rules 901(a)(2)(ii)(A) and 901(a)(2)(ii)(B); Regulation SBSR Adopting Release, 80 FR 14596.

conduct requirements to the U.S. business both of registered foreign security-based swap dealers and of registered U.S. security-based swap dealers, rather than applying the requirements to all transactions of such dealers.[388]

Requiring registered security-based swap dealers to comply with external business conduct requirements with respect to their U.S. business would have two major benefits. First, this requirement would apply to all transactions that constitute U.S. business, as defined under the proposed amendment, requirements that would reduce information asymmetries between security-based swap entities and their counterparties in the security-based swap market in the United States, which should reduce the incidence of fraudulent or misleading representations.[389]

Second, requiring registered foreign security-based swap dealers to comply with external business conduct requirements with respect to their U.S. business should facilitate more uniform regulatory treatment of the security-based swap activity of registered security-based swap dealers operating in the United States.[390] As we discussed above, although other business conduct frameworks (such as broker-dealer regulation) may achieve similar regulatory goals, the

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388 The proposed rules address only the scope of transactions that are subject to the external business conduct requirements; they would not change the substance of those requirements.

389 See Business Conduct Proposal, 76 FR 42452.

390 As discussed above, we recognize that, depending on the business structure that a registered U.S. or foreign security-based swap dealer employs, an intermediary (such as an agent that is a registered broker-dealer) may already be subject to certain business conduct requirements with respect to the registered security-based swap dealer's counterparty in the transaction. See Section IV.E, supra. However, as we also noted above, we think it important that the registered security-based swap dealer itself be subject to Title VII external business conduct requirements with respect to security-based swap transactions that are part of its U.S. business. See id. Because the security-based swap dealer and its agent may allocate between themselves specific responsibilities in connection with these external business conduct requirements, to the extent that these requirements overlap with requirements applicable directly to the agent (for example, in its capacity as a broker), and the dealer allocates responsibility for complying with relevant requirements to its agent, we expect any increase in costs arising from the proposed rules to be mitigated.

availability of exceptions may mean that alternative frameworks may not apply to certain business structures used by registered security-based swap dealers to carry out their business in the United States.[391] Our proposed rules would subject all registered security-based swap dealers engaged in U.S. business to the same external business conduct framework, rather than encouraging a patchwork of business conduct protections under U.S. law that may offer counterparties varying levels of protection with respect to their transactions with different registered security-based swap dealers depending on the business model (or models) that each registered security-based swap dealer has chosen to use in its U.S. business.

We recognize that adjusting the scope of transactions subject to external business conduct requirements may affect the programmatic costs incurred by participants in the security-based swap market. For entities already required to register as security-based swap dealers under current rules, the proposed rules adjust the set of transactions and counterparties to which they must apply external business conduct requirements. To the extent that the proposed rules add counterparties and their transactions to this set, registered security-based swap dealers will incur additional costs for each additional transaction.[392] However, we preliminarily believe that the approach taken in this proposal mitigates some of the commenter concerns with the originally proposed definition of "transactions conducted within the United States" by focusing only on the location of the non-U.S. dealer's market-facing personnel and the personnel of the non-U.S. dealer's agents, and not the location of its counterparties' activity.

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391 See note 202, supra (noting exception from broker-dealer definition for banks).

392 See note 275, supra (citing IIB Letter stating that the application of certain Title VII requirements, including external business conduct standards on the transactions of non-U.S. persons with foreign security-based swap dealers based on activity in the United States when neither counterparty is guaranteed would create "serious operational, legal, and economic difficulties for foreign security-based swap market participants.").

3. Regulatory reporting and public dissemination

Proposed amendments to Regulation SBSR would require certain transactions in connection with a person's dealing activity, where that person arranged, negotiated, or executed the transaction using personnel located in a U.S. branch or office, to be reported to a registered SDR and publicly disseminated. The proposed amendments would also assign reporting duties in certain transactions and further delineate limitations on reporting obligations of non-registered persons engaged in security-based swaps subject to Regulation SBSR. Additionally, the proposed amendments add provisions that would require any security-based swap transaction that is either executed on a platform having its principal place of business in the United States or effected by or through a registered broker-dealer both to be reported to a registered SDR and to be publicly disseminated pursuant to Regulation SBSR.[393]

Public dissemination of security-based swap transaction data may result in several programmatic benefits for the security-based swap market, such as improvements to liquidity and risk allocation by reducing the information asymmetries in a security-based swap market where activity is concentrated among a small number of dealers.[394] Additionally, as noted in the Regulation SBSR Adopting Release, participants in the security-based swap market with better information about the risk characteristics of their security-based swaps will be able to make more efficient investment decisions.[395] To the extent that the provision of security-based swap trade information enables participants in the security-based swap market to make privately optimal decisions, the transaction-level reporting and dissemination requirements will provide

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393 See proposed rule 908(a)(1).

394 See Regulation SBSR Adopting Release, 80 FR 14704.

395 See id.

programmatic benefits in the form of improved liquidity and risk allocation.[396] We preliminarily believe that the proposed amendments would extend these effects by applying post-trade transparency to additional transactions and transaction notional.

Regulatory reporting of transaction data to registered SDRs should enable us to gain a better understanding of the security-based swap market, including the size and scope of that market. This data should enable us to identify exposure to risks undertaken by individual market participants or at various levels of aggregation, as well as credit exposures that arise between counterparties. Additionally, regulatory reporting will help the Commission in the valuation of security-based swaps. Taken together, regulatory data will enable us to conduct robust monitoring of the security-based swap market for potential risks to financial stability.

Regulatory reporting of security-based swap transactions should also improve our ability to oversee the security-based swap market and to detect and deter market abuse. We will be able, for example, to observe trading activity at the level of both trading desk and individual trader, using trading desk IDs and trader IDs, respectively. This ability to aggregate the information contained in registered SDRs using Unique Identification Codes facilitates our ability to examine for noncompliance and pursue enforcement actions as appropriate.

On the other hand, as discussed in the Regulation SBSR Adopting Release, other jurisdictions continue to develop rules related to post-trade transparency of security-based swaps at a different pace, and we are aware that the rules of these other regimes may result in increasing incentives for non-U.S. market participants to avoid contact with U.S. counterparties to avoid effecting transactions by or through registered broker-dealers in an effort to avoid public

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[396] Public transaction data can improve the efficiency of private decisions but there may still remain financial network externalities as discussed in the Cross-Border Adopting Release. See Cross-Border Adopting Release, 79 FR 47284.

dissemination.[397] Responses to these incentives could reduce liquidity for U.S. market participants.[398] We cannot readily quantify the costs that might result from reduced market access for U.S. persons.[399] Moreover, we do not know definitively what rules other jurisdictions may implement or at which time they may implement their rules. In light of these limitations, we have analyzed them qualitatively, and this analysis has informed our formulation of the proposed rules and amendments contained in this release.[400]

Application of regulatory reporting requirements under the proposed amendments to rules 901 and 908 would likely impose costs on non-U.S. persons while providing benefits to the security-based swap market more generally. We preliminarily believe that the approach proposed in this release is responsive to the views of commenters.[401] Under the proposed approach, and in contrast to the original proposal based on "transactions conducted within the United States," non-U.S. persons would not be required to understand or capture whether their non-U.S.-person counterparties use personnel located in the United States, or agents with personnel located in the United States, to determine whether regulatory reporting and public

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397 See Regulation SBSR Adopting Release, 80 FR 14714.

398 See id.

399 We noted in the Regulation SBSR Adopting Release that lack of robust data and lack of experimental conditions make the costs associated with market exit or reduced liquidity that might result from post-trade transparency unquantifiable. The same limitations make the costs of reduced access to liquidity by U.S. persons as a result of public dissemination requirements under the proposed rules and amendments unquantifiable. See Regulation SBSR Adopting Release, 80 FR 14706.

400 See Section II.B.4, supra.

401 See note 275, supra (citing IIB Letter stating that the application of certain Title VII requirements, including the regulatory reporting and public dissemination requirements, on the transactions of non-U.S. persons with foreign security-based swap dealers based on activity in the United States when neither counterparty is guaranteed would create "serious operational, legal, and economic difficulties for foreign security-based swap market participants"); note 288, supra (citing Cleary Letter). See also note 289, supra (citing ISDA Letter, urging us to not apply Regulation SBSR on the basis of conduct within the United States as it would be impracticable).

dissemination requirements are applicable to transaction activity. This modified approach focuses on the location of a non-U.S. dealer's market-facing personnel in determining whether regulatory reporting requirements apply to transaction activity.

Nevertheless, we acknowledge that under the proposed rules and amendments, non-U.S. persons would bear costs of reporting insofar as they are allocated reporting responsibilities within the hierarchy laid out in proposed rule 901(a)(2)(ii)(E), and if they fall within the set of non-U.S. persons whose transactions are required to be reported under rule 908(a). Additionally, registered broker-dealers would incur reporting costs when they are involved in transactions between non-U.S. persons that do not fall within proposed rule 908(b)(5). In the Regulation SBSR Adopting Release, we estimated that 300 parties would incur costs associated with reporting transactions to registered SDRs.[402]

As noted above, we currently lack data necessary to estimate with precision the number of non-U.S. persons that, in connection with their dealing activity, arrange, negotiate, or execute security-based swaps using personnel located in the United States or execute security-based swaps on a platform with its principal place of business in the United States, or the number of registered broker-dealers that intermediate security-based swap transactions, and, as a result, cannot precisely estimate the number of additional non-U.S. persons that might incur reporting obligations under this proposal. However, assuming that all observable transaction activity is arranged, negotiated, or executed using personnel located in the United States, we estimate that 90 persons would become subject to regulatory reporting requirements under the proposed rules,

[402] See Regulation SBSR Adopting Release, 80 FR 14701.

involving approximately 2,700 transactions and $18.5 billion in notional value.[403] Additionally, we preliminarily estimate approximately 30 registered-broker dealers may be involved in effecting transactions between non-U.S. persons that would not incur any reporting duties under Regulation SBSR.

We preliminarily believe that regulatory reporting of transactions that are arranged, negotiated, or executed using personnel located in a U.S. branch or office or effected through a registered broker-dealer would have benefits for the security-based swap market. Increasing the scope of security-based swap transactions subject to regulatory reporting would likely extend the programmatic benefits of regulatory reporting discussed in the Regulation SBSR Adopting

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403 Commission staff arrived at these estimates by constructing a sample of TIW transaction records for activity between two counterparties in 2014, removing those records that involve counterparties that appear likely to register as security-based swap dealers, to isolate activity that would likely fall within the scope of proposed rule 901(a)(2)(ii)(E)(3). Staff arrived at numerical estimates by counting unique TIW accounts, transaction counts, and transaction notional represented in this sample. This revealed approximately 45 accounts and approximately 1,650 transactions, involving $8.3 billion in notional value. As in prior releases, we preliminarily believe it is appropriate to take a conservative approach and estimate an upper bound of 90 affected persons to account for growth in security-based swap participation. See Intermediary Definitions Adopting Release, 77 FR 30725 n.1457.

Further, we preliminarily believe it is reasonable to increase our estimates of transaction counts and notional volume by a factor of 1.6 to account for data limitations. First, our access to single-name CDS data is limited to activity involving one U.S. counterparty or involving CDS written on U.S. reference entities. We estimated that this limitation prevents us from observing approximately 23% of transactions. See Regulation SBSR Adopting Release, 80 FR 14689 n.1183. Second, as we note in Section II.B.1, when measured in terms of notional outstanding, the single-name CDS market accounts for approximately 80% of the overall security-based swap market. As a result, we scale up the number of observed transactions first by 1/(1-0.23) and then by 1/0.80, or to approximately 1650 x 1/0.77 x 1/0.80 = 2679 transactions, and our estimate of notional volume to approximately $8.3 billion x 1/0.77 x 1/0.80 = $13.5 billion. We acknowledge that this scaling rests on an implicit assumption that transactions we do not observe are similar in nature to the single-name CDS transaction we do observe.

Further we assume that 20% of these transactions would be reported by registered-broker dealers pursuant to 901(a)(2)(ii)(E)(4) and so no reporting of life-cycle events would be required. We use data in the Regulation SBSR Adopting Release to develop our estimate of the number of events that are not life-cycle events. See Regulation SBSR Adopting Release, 80 FR 14702.

Release by giving us a more complete view of transactions activity within the United States.[404] Moreover, in the context of market surveillance, regulatory reporting of these transactions may be particularly valuable. For example, these regulatory data would allow us to sequence all security-based swap transaction activity involving U.S. personnel. This potentially allows detection of cases in which U.S. personnel could exploit their private information about the order flow of their clients by placing proprietary orders ahead of clients' orders as an employee of a non-U.S. affiliate, avoiding regulatory reporting requirements under Regulation SBSR. Such a strategy could involve front-running orders in an opaque part of the security-based swap market at the expense of participants in a more transparent market. Monitoring for these types of activities would be more difficult in the absence of the proposed amendments to Rule 908. Finally, by requiring registered broker-dealers to report transactions in which they are involved, we preliminarily believe that our proposed approach to regulatory reporting would enable us to improve oversight of registered broker-dealers.

Regulatory reporting and public dissemination of transaction data may entail two types of costs for security-based swap market participants. First, as detailed below, requiring non-U.S. persons with dealing activity in the United States to comply with the Title VII reporting requirements even if they are not registered security-based swap dealers may entail additional costs for recordkeeping, supervision, and compliance. As some portion of these costs may be fixed, security-based swap market participants with smaller volume may be more adversely affected than larger ones. A second type of cost may fall on non-U.S. persons, including registered foreign security-based swap dealers, that wish to execute large orders or execute orders in particularly illiquid contracts. Public dissemination of these types of transactions,

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404 See Regulation SBSR Adopting Release, 80 FR 14700.

either because they involve security-based swap dealing activity in the United States or because they are effected through a registered broker-dealer, may increase the costs of hedging the inventory risk generated by such transactions because it may signal the direction of future order flow to potential counterparties to hedging transactions. As we noted in the Regulation SBSR Adopting Release, staff analysis of recent transactions in single-name CDS suggests that the impact of public dissemination on large transactions may be limited in light of the interim approach to public dissemination that allows up to a 24-hour delay before transactions data is made public.[405]

The proposed amendments to Rule 901 would assign reporting duties in certain transactions and we preliminarily believe that these duties would result in costs for U.S. and non-U.S. persons and registered broker-dealers (including registered SB SEFs) that incur a duty to report. We estimated the costs of reporting on a per-entity basis in the Regulation SBSR Adopting Release and we preliminarily believe that these proposed rules would not affect these costs. We preliminarily believe that additional persons required to report by the proposed amendments would incur costs associated with establishing internal order management systems of approximately $102,000. These entities with reporting duties would also have to establish and maintain connectivity to a registered SDR at a cost (initial and ongoing) of approximately $200,000. We preliminarily believe that these persons would incur costs associated with establishing a reporting mechanism for security-based swaps of approximately $49,000. We preliminarily estimate that the ongoing costs of internal order management would be $77,000 per year, per reporting side, and the annual and ongoing costs of storage of $1,000 per year, per

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405 See Regulation SBSR Adopting Release, 80 FR 14709. See also "Inventory risk management by dealers in the single-name credit default swap market" (October 17, 2014, available at: http://www.sec.gov/comments/s7-34-10/s73410-184.pdf).

reporting side. The Commission preliminarily believes that under the proposed amendments, entities with reporting duties would incur costs of approximately $54,000 per reporting side to establish an appropriate compliance and support program for regulatory reporting. We further estimate that such a program would require approximately $38,500 per year in annual spending by each reporting side. In aggregate, the costs of rule 901 for persons required to report under the proposed amendments in the first year would be approximately $521,500 and the annual ongoing costs would be approximately $316,500.[406] In aggregate, this suggests first-year costs of approximately $62.5 million and ongoing costs of approximately $38 million.[407]

As discussed in the Regulation SBSR Adopting Release, we preliminarily estimated and continue to believe that the burden of reporting additional transactions once a respondent's reporting infrastructure and compliance systems are in place would be minimal when compared to the costs of putting those systems in place and maintaining them over time.[408] If firms have order management systems in place and currently utilize them, the costs of reporting an additional individual transaction would be entering the required data elements into the firm's order management system, which could subsequently determine whether regulatory reporting requirements apply to the transaction, and deliver the required transaction information to a registered SDR if required.[409]

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406 See Regulation SBSR Adopting Release, 80 FR 14702.

407 First-year costs of $521,500 x 120 entities with reporting duties = $61,580,000; ongoing costs of $316,500 x 120 entities with reporting duties = $37,980,000. These costs may be mitigated to the extent that a registered broker-dealer may use the infrastructure separately established by an affiliate that already incurs reporting obligations under Regulation SBSR.

408 See Regulation SBSR Adopting Release, 80 FR 14702.

409 See id.

Besides incurring costs in connection with reporting responsibilities under rule 901, we preliminarily believe that the proposed rules would also require certain non-U.S. persons and registered broker-dealers to incur costs associated with error reporting under rule 905. As we noted in the Regulation SBSR Adopting Release, requiring participants to promptly correct erroneous transaction information should help ensure that the Commission and other relevant authorities have an accurate view of the risks in the security-based swap market. We preliminarily believe that non-U.S. persons that incur reporting obligations under the proposed amendments would incur an initial cost of $11,825 per reporting side and an ongoing cost of $4,000 per reporting side.[410]

These figures suggest aggregate initial costs of $1,419,000 and ongoing costs of $480,000.[411] As with rule 901, as adopted, we do not believe that the additional amendments made to rule 901 in this release would have any measurable impact on the costs previously discussed in both the Regulation SBSR Proposing Release and the Cross-Border Proposing Release.[412]

We preliminarily believe that, in addition, the 540 additional transactions effected by or through registered broker-dealers may impose costs on participants that are associated with notifying registered broker-dealers after discovery of an error as required under rule 905(a)(1).

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410 See id. at 14778. Note that we preliminarily believe that this proposal does not alter the number of participants that are not reporting sides who, under rule 905(a)(1), are required to notify the relevant reporting side after discovery of an error.

411 Initial costs of $11,825 x 120 entities with reporting duties = $1,419,000; ongoing costs of $4,000 x 120 entities with reporting duties = $480,000.

412 See Regulation SBSR Adopting Release, 80 FR 14702. See also Regulation SBSR Proposing Release, 75 FR 75261; Cross-Border Proposing Release, 78 FR 31192.

We preliminarily estimate an annual cost associated with this obligation of approximately $17,280, which corresponds to roughly $576 per participant.[413]

Finally, the proposed amendments to rule 906 may impose costs on registered broker-dealers that must report transactions to satisfy an obligation under proposed rule 901(a)(2)(ii)(E)(4). Under proposed amendments to rule 906(c), these registered broker-dealers would be required to establish, maintain, and enforce policies and procedures that are reasonably designed to ensure that it complies with any obligations to report information to a registered SDR in a manner consistent with Regulation SBSR. Further, these registered broker-dealers would be required to review these policies and procedures at least annually. We preliminarily estimate that the cost associated with establishing such policies and procedures would be approximately $58,000 and the cost associated with annual updates would be approximately $34,000, for each registered broker-dealer that incurs an obligation to report transactions under our proposed approach.[414]

4. Efficiency, competition, and capital formation

Our analysis of the proposed rules' potential impacts on efficiency, competition, and capital formation begins by considering the effects the proposed rules may have on the scope of participants subject to dealer requirements under Title VII. Following this discussion, we

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413 These figures are based on the assumption that approximately 540 additional trades per year would have to be reported by registered broker-dealers pursuant to proposed rule 901(a)(2)(ii)(E)(4) and that these trades involve 30 entities with reporting duties. Using cost estimated provided in the Regulation SBSR Adopting Release, if each trade is reported in error, then the aggregate annual cost of error notification is 540 errors x Compliance Clerk at $64 per hour x 0.5 hours per report = $17,280, or $576 per participant. See Regulation SBSR Adopting Release, 80 FR 14714. We use salary figures from SIFMA's Management & Professional Earnings in the Securities Industry 2013, modified by SEC staff to account for a 1800-hour work-week and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

414 See Regulation SBSR Adopting Release, 80 FR 14716.

examine potential effects of the proposed rules related to their effect on the application of Regulation SBSR.

We note that the proposed rules and amendments would, if adopted, affect the security-based swap market in a number of ways, many of which are difficult to quantify, if not unquantifiable. In particular, a number of the potential effects that we discuss below are related to price efficiency, liquidity and risk sharing. These effects are difficult to quantify for a number of reasons. First, in many cases the effects are contingent upon strategic responses of market participants. For instance, we note in Section VI.B.4(b)i, infra, that, under our proposed approach, non-U.S. persons may choose to relocate personnel making it difficult for U.S. counterparties to access liquidity in security-based swaps. The magnitude of these effects on liquidity and on risk sharing depend upon a number of factors that we cannot estimate, including the likelihood of relocation, the availability of substitute liquidity suppliers and the availability of substitute hedging assets. Therefore, much of the discussion below is qualitative in nature, although we try to describe, where possible, the direction of these effects.

Not only can some of these effects be difficult to quantify, but there are many cases where a rule will have two opposing effects, making it difficult to estimate a net impact on efficiency, competition, or capital formation. For example, in our discussion of the net effect of the proposed application of Regulation SBSR requirements on efficiency, we expect that post-trade transparency may have a positive effect on price efficiency, while it may negatively affect liquidity by providing incentives for non-U.S. persons to avoid contact with U.S. persons. The magnitude of these two opposing effects will depend on factors such as the sensitivity of traders to information about order flow, the impact of public dissemination of transaction information on the execution costs of large orders, and the ease with which non-U.S. persons can find substitutes

that avoid contact with U.S. personnel. Each of these factors is difficult to quantify individually, which makes the net impact on efficiency equally difficult to quantify.

(a) De minimis calculations

The proposed rules and amendments related to the treatment of transactions arranged, negotiated, or executed by personnel located in the United States for the purposes of de minimis calculations likely broadens the scope of security-based swap transactions and entities to which the Title VII regulatory regime for security-based swap dealers applies. As a result, the proposal may increase the effects on efficiency, competition, and capital formation of rules already adopted as well as of future substantive rulemakings that place responsibilities on registered security-based swap dealers to carry out entity- or transaction-level requirements applicable to security-based swap dealers under Title VII.[415]

The proposed rules and amendments may directly affect efficiency, competition, and capital formation because the requirement that non-U.S. persons include in their de minimis threshold calculations security-based swaps in connection with their dealing activity that they arrange, negotiate, or execute using personnel located in a U.S. branch or office may increase the likelihood that certain non-U.S. dealers would exceed de minimis levels of dealing activity and be required to register with the Commission. Registration would cause these dealers to incur registration costs as well as the costs of dealer requirements under the Title VII regulatory regime.

These costs may represent barriers to entry for non-U.S. persons that contemplate engaging in dealing activity using their own personnel or personnel of their agents located in a U.S. branch or office or provide incentives for non-U.S. persons that currently engage in relevant

[415] See Cross-Border Adopting Release, 79 FR 47361.

activity using personnel located in a U.S. branch or office to restructure their business and move operations abroad or use agents with personnel outside of the U.S.[416] These costs may additionally provide direct incentives for non-U.S. persons to avoid using personnel of agents located in a U.S. branch or office (or agents with such personnel) to arrange, negotiate or execute security-based swaps on their behalf. By reducing the ability of these agents to compete for business from non-U.S. persons, the proposed rules may reduce entry by potential agents because of this competitive disadvantage, or cause existing agents to relocate or restructure their business to minimize contact with the United States.[417]

We acknowledge that, to the extent that it occurs solely for the purposes of avoiding Title VII regulation, reduced market entry or restructuring by non-U.S. persons responding to our proposed approach, or by agents unable to compete for business from non-U.S. persons, may be inefficient, raise costs to market participants and reduce the level of participation by personnel of non-U.S. persons located in the United States, or personnel of their agents located in the United States.[418] Our proposed approach reflects consideration of the potentially inefficient restructuring and reduced access to the security-based swap market by U.S. persons on the one hand, and addressing the concerns of Title VII on the other. In particular, this proposed approach potentially reduces the risk of financial contagion and fraudulent or manipulative conduct by ensuring that security-based swap dealer regulation is applied to the appropriate set of entities whose activities raise these concerns.

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416 See id. at 47362.

417 We also note that, under the proposed rules, non-U.S. persons may be willing to pay higher prices for higher quality services provided by non-U.S.-person counterparties that use personnel or agents located in the United States because the ability of these counterparties to meet the standards set by Title VII may be a credible signal of high quality. See id. at 47362 n.762.

418 See id. at 47364.

We also preliminarily believe that the proposed rules and amendments would affect competition among security-based swap dealers. Under proposed Exchange Act rule 3a71-3(b)(iii)(C), U.S. persons would have to count their dealing activity towards their de minimis thresholds while their non-U.S. competitors would not. As noted in Section II.A, supra, in the absence of the proposal, a U.S. person engaged in dealing activity and facing a non-U.S.-person counterparty or its agent would face different regulatory treatment from a non-U.S. person engaged in the same activity with the same counterparty or its agent, even if both are arranging, negotiating, or executing the security-based swap using personnel located in a U.S. branch or office. As a result, and as noted by commenters,[419] current rules may introduce different costs for U.S. security-based swap dealers and foreign security-based swap dealers and their agents that seek to supply liquidity to non-U.S. persons as a result of Title VII regulation, introducing competitive disparities even if the U.S. person and the non-U.S. person or their agents are both, in connection with their dealing activity, using personnel located in the United States. Under the current rules, non-U.S. persons seeking or supplying liquidity may also be reluctant to transact with a U.S. person because of the additional expected costs of dealer regulation and of future substantive regulations under Title VII that rest on the U.S.-person status of counterparties. We preliminarily believe that many of the costs of these frictions would be borne by U.S. security-based swap dealers. The proposed rules and amendments may mitigate these competitive frictions because non-U.S. persons would be required to count transactions arranged, negotiated,

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419 See note 196, supra (citing IIB Letter and SIFMA/FIA/FSR Letter raising concerns that the proposed rule could put U.S. brokers and investment managers at a competitive disadvantage). See also note 138, supra (citing AFR Letter to CFTC); notes 139 and 299, supra (citing CDEU Letter to CFTC); note 131, supra (citing ISDA Letter to CFTC and SIFMA/FIA/FSR Letter to CFTC); note 142, supra (citing Société Générale Letter to CFTC); note 143, supra (citing JFMC Letter to CFTC, CDEU Letter to CFTC, SIFMA/FIA/FSR Letter to CFTC, and IAA Letter to CFTC); note 300, supra (citing ISDA Letter to CFTC). See also note 101, supra.

or executed by personnel located in a U.S. branch or office towards their de minimis thresholds in a way that is identical to their U.S.-person competitors.[420]

As with the proposed amendment that would require non-U.S. persons to count transactions arranged, negotiated, or executed by personnel located in a U.S. branch or office towards de minimis thresholds, the proposal does not retain an exception for cleared, anonymous transactions and thus should reduce the competitive frictions that would exist if the proposal retained the exception. Such an exception would provide non-U.S.-person dealers that arrange, negotiate, or execute cleared, anonymous transactions using personnel located in a U.S. branch or office or using agents with personnel in a U.S. branch or office a potential competitive advantage relative to U.S. persons, as the non-U.S. persons would be able to avoid including these transactions in their de minimis calculations, while U.S. persons would be required to count all such transactions towards their de minimis thresholds. However, we also note that, to the extent that non-U.S. persons otherwise would have relied upon this exception to engage in cleared, anonymous transactions, our proposed approach may impair efficiency and capital formation by reducing liquidity in anonymous markets, increasing transaction costs, and reducing opportunities for risk-sharing among security-based swap market participants.[421]

Alternatively, the proposed rule may result in inefficient restructuring to move the arrangement, negotiation, and execution of cleared, anonymous transactions abroad, in order to avoid activities that would require counting towards de minimis thresholds. This may have adverse consequences for the availability of liquidity and the amount of transaction costs for U.S. persons seeking to hedge risk using security-based swaps. If non-U.S. persons relocate their

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420 See Cross-Border Proposing Release, 78 FR 31127; Cross-Border Adopting Release, 79 FR 39152.

421 See Cross-Border Adopting Release, 79 FR 47363.

dealing activity abroad in ways that make it difficult for U.S. persons to find liquidity in the United States, those U.S. persons that might otherwise use security-based swaps to hedge financial and commercial risks may reduce their hedging activity and assume an inefficient amount of risk, or engage in precautionary savings that inhibits capital formation.[422] To the extent that non-U.S. persons use U.S. personnel to engage in dealing activity only in a subset of security-based swaps, such as those involving certain reference entities, we preliminarily believe that the potential consequences of relocation on liquidity and risk sharing would be most concentrated in this subset.

(b) Other Title VII requirements

The proposed rules regarding the regulatory reporting, public dissemination and external business conduct requirements for transactions arranged, negotiated, or executed by personnel located in a U.S. branch or office would have several effects on efficiency, competition, and capital formation in the U.S. financial market. These effects implicate common economic themes and warrant a consolidated discussion.

i. Efficiency

The application of public dissemination as set forth in the proposed rule may improve the efficiency of the price discovery process and improve the liquidity of traded security-based swaps. Market participants with more information about the history of prices due to enhanced post-trade transparency will be better able to price security-based swaps, and as a result make better trading decisions. Market observers will be able to incorporate information from the security-based swap market to derive valuations for other assets that are more accurate.[423]

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422 See note 143, supra (citing CDEU Letter to CFTC).

423 See Regulation SBSR Adopting Release, 80 FR 14720.

We preliminarily believe that the magnitude of these efficiency improvements is related to the number of transactions subject to public dissemination. Data from more transactions may allow market participants and observers to derive more precise estimates of fundamental value. As a result, to the extent that the proposed rules increase the scope of security-based swap transactions subject to public dissemination, they may result in more efficient pricing and valuation within and without the security-based swap market.[424]

At the same time, we recognize that particular Title VII requirements may affect efficiency through their effects on the ability of security-based swap market participants to access liquidity. We preliminarily believe that certain aspects of our proposal should reduce the likelihood of market fragmentation. For example, the proposed rules and amendments, by reducing the likelihood that transactions arranged, negotiated, or executed within the United States are subject to disparate levels of regulation under Title VII depending on counterparty identity, the proposed rules may allow U.S. persons to more freely access liquidity made available through dealing activity within the United States and may discourage the formation of a two-tier market in which U.S. persons and non-U.S. persons are offered liquidity on very different terms.

However, we also acknowledge that the proposed rules may provide incentives for non-U.S. persons to move their operations and personnel abroad to avoid external business conduct, regulatory reporting, and public dissemination requirements. If, under the proposed rules, non-

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[424] See Gjergji Cici, Scott Gibson, and John J. Merrick, Jr., "Missing the Marks? Dispersion in Corporate Bond Valuations Across Mutual Funds," Journal of Financial Economics, Volume 101, Issue 1 (July 2011), at 206-26 (providing evidence that the implementation of post-trade transparency in the corporate bond market could have contributed to a reduction in the dispersion of mutual fund valuations during the study's sample period). See also Sugato Chakravarty, Huseyin Gulen, and Stewart Mayhew, "Informed Trading in Stock and Option Markets," Journal of Finance, Vol. 59, No. 3 (2004) (estimating that the proportion of information about underlying stocks revealed first in option markets ranges from 10% to 20%).

U.S. security-based swap market participants relocate their sales forces and trading desks to other jurisdictions, less liquidity may be available within the United States, reducing the efficiency of prices and risk sharing. U.S. counterparties may find it difficult to take desired positions in security-based swaps if their access to non-U.S. liquidity providers is limited or more costly. For example, if U.S. persons seeking to hedge risk using security-based swaps have difficulty obtaining liquidity solely from U.S. providers, they may reduce their hedging activity in the security-based swap market, seek substitutes in other asset markets, or assume an inefficient amount of risk.[425] We note that the incentive to relocate personnel may grow to the extent that there is a substantial disparity in regulatory requirements applicable to those transactions that are arranged, negotiated, or executed by personnel from a location within the United States and those transactions that are not.

As an alternative to relocating personnel, we acknowledge that participants may implement or adapt existing controls or conventions that restrict communication between non-U.S. trading personnel and persons located in the United States to avoid triggering certain Title VII requirements. For example, firms may adopt policies restricting personnel located outside the United States from communicating with personnel located in the United States when engaging in dealing activity with non-U.S.-person counterparties. Non-U.S. firms might additionally restrict personnel located in the United States from arranging, negotiating, or executing security-based swaps in connection with the non-U.S. firm's dealing activity with non-U.S.-person counterparties.

Although non-U.S. persons may voluntarily impose internal conventions and controls on their own personnel to avoid triggering certain Title VII requirements, these conventions and

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[425] See note 143, supra (citing CDEU Letter to CFTC).

controls may result in inefficient duplication of personnel or expertise in foreign and U.S. locations. Non-U.S. persons may choose to impose controls on personnel if the costs of duplication are below the costs of applying Title VII to relevant activity,[426] but we preliminarily believe that such a strategic choice may not take into account the programmatic benefits of Title VII regulation. For example, public dissemination requirements under Title VII improve the transparency of the security-based swap market while causing market participants and SDRs to incur costs. Other portions of the Title VII regulatory framework, such as capital and margin requirements yield programmatic benefits by reducing the risk of sequential counterparty default, but security-based swap dealers may consider the impact of such requirements on their own costs, without considering impacts on aggregate financial sector risk.[427] Thus, although internal personnel controls may be privately optimal for firms that choose to implement them, their net impact on efficiency will depend on how the costs of personnel duplication compare to the overall costs and benefits of the Title VII dealer regulation, external business conduct, regulatory reporting, and public dissemination requirements.

Similarly, we preliminarily believe that our proposed approach more consistently applies

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426 See Section VI.A (discussing the estimated per-entity costs of these controls).

427 See e.g. Daron Acemoglu, Asuman Ozdaglar & Alireza Tahbaz-Salehi, Systemic Risk and Stability in Financial Networks (NBER Working Paper No. 18727, Jan. 2013), available at: http://www.nber.org/papers/w18727 (showing the emergence of financial network externalities in a theoretical model of banks, in which banks may take into account the effect of their own risk taking on their creditors, but may fail to internalize the effects of their own risk taking on their creditors' creditors).

See also Viral V. Acharya, Lasse H. Pedersen, Thomas Philippon, and Matthew Richardson, "Measuring Systemic Risk" (May 2010), available at: http://vlab.stern.nyu.edu/public/static/SR-v3.pdf. (using a theoretical model of the banking sector to show that, unless the external costs of their trades are considered, financial institutions will have an incentive to take risks that are borne by the aggregate financial sector). Under this theory, in the context of Title VII, the relevant external cost is the potential for risk spillovers and sequential counterparty failure, leading to an aggregate capital shortfall and breakdown of financial intermediation in the financial sector.

regulatory reporting and public dissemination requirements to transactions effected by or through trading platforms and registered broker-dealers, including registered SB SEFs. Both trading platforms and registered broker-dealers may intermediate transactions in the security-based swap market. By ensuring that both types of intermediation are subject to regulatory reporting and public dissemination requirements, the proposed approach reduces the risk that, as a result of disparate treatment, liquidity migrates from trading platforms to registered broker-dealers or from registered broker-dealers to trading platforms. However, at the same time, we acknowledge the risk that, in response to the proposed rules and amendments, trading platforms may choose to move their principal place of business offshore and registered broker-dealers may move their security-based swap businesses into unregistered entities to avoid regulatory reporting requirements.

Attempts to restructure by counterparties, trading platforms and registered broker-dealers could have an adverse effect on the efficiency of the security-based swap market by fragmenting liquidity between a U.S. security-based swap market, occupied by U.S. persons and non-U.S. persons willing to participate within the Title VII regulatory framework, with intermediation services provided by registered broker-dealers and U.S.-based trading platforms, and an offshore market whose participants seek to avoid any activity that could trigger application of Title VII to their security-based swap activity.[428] Such market fragmentation could reduce the amount of liquidity available to market participants whose activity is regulated by Title VII and significantly erode any gains in price efficiency and allocative efficiency that might result from pre- and post-trade transparency.

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[428] See Cross-Border Adopting Release, 79 FR 47364.

ii. Competition

We preliminarily believe that our proposed approach would have implications for competition among market participants that intermediate transactions in security-based swaps as well as counterparties to security-based swaps. First, the proposed rules and amendments to rules 901 and 908 would apply consistent regulatory reporting and public dissemination requirements to transactions between non-U.S. persons that are platform-executed or effected through registered broker-dealers. We preliminarily believe that our proposed application of regulatory requirements is unlikely to generate competitive frictions between these different types of providers of intermediation services. At the same time, we acknowledge that proposed rule 908(a)(1)(iv) may make it difficult for suppliers of intermediation services (i.e., trading platforms and broker-dealers) effecting or executing transactions within the United States, to compete to serve non-U.S. persons. Nonetheless, we preliminarily believe that our proposed approach would appropriately reflect the transparency focus of Title VII and would promote a robust regulatory regime for registered broker-dealers.

Applying external business conduct requirements and Regulation SBSR to transactions in connection with a non-U.S. person's dealing activity that the non-U.S. person arranges, negotiates, or executes using personnel located in the United States would mitigate competitive frictions between U.S. and non-U.S. persons[429] by providing for a generally consistent application of these requirements to U.S.-person dealers and non-U.S.-person dealers or their agents to the extent that the latter arrange, negotiate, or execute a security-based swap transaction

[429] Competitive effects would flow from each of the relevant Title VII requirements. For instance, post-trade transparency may increase competition between dealers by reducing the level of private information that large dealers have relative to smaller dealers and by improving the ability of non-dealers to negotiate with dealers on prices. See Regulation SBSR Adopting Release, 80 FR 14704.

in connection with their dealing activity using personnel located in a U.S. branch or office.[430] If only U.S. dealers and their agents were subject to disclosure requirements with respect to their security-based swap transactions, the costs of such disclosures would primarily affect U.S. dealers, their agents, and their counterparties. In contrast, non-U.S. dealers and their agents, who may not necessarily be subject to comparable disclosure requirements, could have a competitive advantage over U.S. dealers in serving non-U.S.-person counterparties using personnel located in a U.S. branch or office, were their activities not subject to the same requirements.[431] Furthermore, we preliminarily believe the ability to meet certain Title VII regulatory requirements under the proposed rules may allow non-U.S. persons who use personnel or personnel of agents located in the United States to engage in dealing activity to credibly signal high quality and better counterparty protection relative to other non-U.S. persons that compete for the same order flow from weaker regulatory environments.[432] Non-U.S. persons that choose to use personnel or personnel of agents for dealing activity from a location within the United States may find fraud or abusive behavior more costly and difficult to conduct, which may signal to other non-U.S. persons that such fraud or abusive behavior is unlikely to occur.

We are not proposing, however, to apply the clearing and trade execution requirements to security-based swap transactions that a non-U.S. person, in connection with its dealing activity, arranges, negotiates, or executes using personnel located in a U.S. branch or office. This aspect

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430 See Cross-Border Proposing Release, 78 FR 31127; Cross-Border Adopting Release, 79 FR 47327 (providing earlier discussions of these issues).

431 See, e.g., Arnoud W.A. Boot, Silva Dezelan, and Todd T. Milbourn, "Regulatory Distortions in a Competitive Financial Services Industry," Journal of Financial Services Research, Vol. 17, No. 1 (2000) (showing that, in a simple industrial organization model of bank lending, a change in the cost of capital resulting from regulation results in a greater loss of profits when regulated banks face competition from unregulated banks than when regulations apply equally to all competitors).

432 See Cross-Border Adopting Release, 77 FR 47362 n.762.

of our proposal may contribute to a disparity in the regulatory treatment of U.S. persons and non-U.S. persons in the security-based swap market, as non-U.S. persons that engage in dealing activity using personnel located in the United States would only be subject to Title VII dealer regulation and Regulation SBSR, while U.S. persons would also be required to comply with the clearing and trade execution requirements. If clearing and trade execution requirements comprise a large portion of the Title VII compliance costs, then a competitive disparity between U.S. and non-U.S. participants in the security-based swap market may remain, even with the addition of the proposed rules. However, to the extent that U.S. persons and non-U.S. persons whose obligations under a security-based swap are guaranteed by U.S. persons must increase the price of the liquidity they supply in response to this disparity in regulatory treatment, we preliminarily believe that these higher prices reflect an efficient allocation of the costs their activity may impose on the U.S. financial system, given that the counterparty credit risk of such security-based swap transactions resides primarily in the United States.

iii. Capital Formation

The proposed rules may affect capital formation in the security-based swap and securities market by affecting the transparency, liquidity, and stability of the market. Requiring transactions by non-U.S. persons, in connection with their dealing activity, with relevant activity in the United States to be reported and publicly disseminated should facilitate monitoring of the security-based swap market and improve the price discovery process and the liquidity of security-based swaps.[433] These improvements may lead to more efficient allocation of capital by market participants and market observers, facilitating capital formation.

[433] See Regulation SBSR Adopting Release, 80 FR 14719-722.

We recognize that the effects of the proposed rule on market fragmentation may affect capital formation. If the proposed rules reduce the likelihood of fragmentation of the security-based swap market, then they may promote capital formation. Under a regulatory environment that facilitates U.S. persons' access to the global security-based swap market, U.S. market participants will be able to more efficiently hedge financial and commercial risks, reducing the level of precautionary savings they choose to hold and instead investing resources in more productive assets. However, if the proposed rules cause non-U.S. persons to move personnel and operations abroad or use agents operating outside the United States, the costs of the move represent resources that could have been invested in productive assets. Furthermore, to the extent that such restructuring results in a fragmented market with reduced liquidity for security-based swaps and related assets within the United States, the result could be less risk sharing and impaired capital formation.[434]

5. Request for comment

The Commission requests comment on all aspects of our discussion and analysis concerning programmatic costs and benefits, and potential impacts, of the proposed rule on efficiency, competition, and capital formation, including the following:

- Does our discussion above accurately characterize, qualitatively and quantitatively, the incentives for entities to restructure in the absence of, or as a result of, the proposed rules? Please explain and provide information that would be helpful in performing further analysis.
- Does our discussion above accurately characterize, qualitatively and quantitatively, the benefits and costs of application of external business conduct

[434] See Cross-Border Adopting Release, 79 FR 47365.

requirements to transactions with dealing activity by personnel from a location within the United States? Please explain and provide information that would be helpful in performing further analysis.

- Our proposal does not retain an exception for cleared, anonymous transactions that would exclude these from the de minimis calculations for non-U.S. persons. Please provide information that would be helpful in estimating any effects of this approach on liquidity on platforms that support anonymous trading.
- Does our discussion above accurately characterize, qualitatively and quantitatively, the benefits and costs of application of Title VII requirements to transactions between two non-U.S. persons in which at least one of the non-U.S. persons, in connection with its security-based swap dealer activity, arranges, negotiates, or executes the security-based swap using personnel located in the United States? Please explain and provide information that would be helpful in performing further analysis.

C. Alternatives Considered

In developing these proposed rules and amendments we considered a number of alternative approaches. This section outlines these alternatives and discusses the potential economic effects of each.

1. Retention of the definition of "transaction conducted within the United States"

In the Cross-Border Proposing Release, we originally proposed the definition "transaction conducted within the United States" and used it to identify (i) transactions that should be included in an entity's de minimis threshold calculations, and (ii) transactions that, subject to certain exceptions, would be subject to the set of Title VII requirements for business

conduct, clearing, trade execution, regulatory reporting, and public dissemination. The original objective of the initial definition was identical to this proposed rule—to capture relevant dealing activity within the United States in order to mitigate competitive frictions and prevent a non-U.S. person from shifting its security-based swap dealing activity to a non-U.S. person and continue to carry out this dealing activity in the United States while avoiding application of the Title VII requirements by using personnel of the non-U.S. person located in the United States or personnel of its agent located in the United States.

We have determined to propose a different approach in part because we preliminarily agree with commenters that the initial approach likely would have increased assessment costs significantly.[435] That initial approach would have looked to whether dealing activity involved a "transaction conducted within the United States," which, as defined in that proposal, turned on the location of personnel on both sides of the transaction. Accordingly, under the rule as initially proposed, an entity would have been required to include a transaction in its de minimis threshold calculations based on the location of its counterparty's personnel. Gathering such information, communicating it to relevant counterparties, and keeping records of this information on a per-transaction basis could be costly. We preliminarily believe that our re-proposed approach, which focuses only on whether the non-U.S. person is arranging, negotiating, or executing a security-based swap, in connection with its dealing activity, using personnel located in a U.S. branch or office, achieves many of the same programmatic benefits, while resulting in in lower assessment costs.[436]

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[435] See, e.g., note 289, supra (citing ISDA Letter).

[436] As we noted in Section III.B.2, supra, some commenters urged that an activity-based test should look only to where the relevant transaction was executed or where the dealer's personnel committed the dealer to that trade. Although we acknowledge that such an alternative may result

2. Limited exception from Title VII requirements for transactions arranged, negotiated, and executed by associated persons of broker-dealers

We also considered not requiring a non-U.S. person to include a transaction in its de minimis threshold calculations if the security-based swap dealing activity was arranged, negotiated, or executed in the United States solely by personnel of a registered broker-dealer that were acting in their capacity as associated persons of that broker-dealer. One commenter suggested such an approach.[437] Although this approach could reduce costs associated with engaging in customer-facing activity in connection with dealing activity in security-based swaps in the United States, it would, as described in more detail above,[438] create potentially significant compliance gaps in our Title VII framework, potentially impeding our effective enforcement of Title VII and other federal securities laws by reducing the number of transactions carried out by registered security-based swap dealers and thus limiting our access to the books and records that are necessary for effective enforcement.

3. Exclusion of security-based swap transactions that do not involve a U.S.-person counterparty, a counterparty whose obligations under the security-based swap are guaranteed by a U.S. person, or a conduit affiliate from the de minimis threshold requirements

Although the Cross-Border Adopting Release stated that we contemplated considering whether to subject certain security-based swap transactions involving activity in the United States to certain Title VII requirements, one alternative to the proposed rules would be not to require any transactions other than those required in rule 3a71-3 to be counted toward a person's

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in costs that are meaningfully lower than the costs of our proposed approach, because we do not believe that such an alternative would adequately capture the range of market-facing activities that appear likely to raise the types of concerns addressed by security-based swap dealer regulation, we do not believe that this approach reflects a reasonable alternative to the proposed approach.

437 See note 197, supra (citing IIB Letter).

438 See Section III.B.5(c), supra.

dealer de minimis threshold. However, in our preliminary view, in the absence of some form of activity-based test, the current scope of rules may not adequately address fraud and competitive fragmentation concerns. Further, personnel located in a U.S. branch or office may be employed by both U.S. and non-U.S. persons. Absent an activity-based test, our ability to enforce relevant regulations may be hindered by our inability to monitor the activity of such personnel carried out in their role as employee of the non-U.S. person.

The absence of an activity-based test may also adversely affect competition between U.S. and non-U.S. persons. Under current rules, the disparity in regulatory treatment means U.S. and non-U.S. persons will face disparate regulatory costs even if both engage in dealing activity using personnel located in a U.S. office. Non-U.S. persons or their agents transacting with other non-U.S. persons or their agents in the United States would potentially be able to provide liquidity at lower cost than U.S. persons because of differing regulatory treatment in other jurisdictions. As a result, non-U.S. persons could prefer to transact with non-U.S. persons or their agents, and a substantial portion of liquidity from non-U.S. persons may become unavailable to U.S. persons.

4. Extension of the activity-based test to the clearing and execution requirements

As we discuss above in Section V.D, we are not proposing to require mandatory clearing or mandatory trade execution for security-based swap transactions that are arranged, negotiated, or executed using personnel located in a U.S. branch or office.[439] Under this alternative, we would subject all transactions arranged, negotiated, or executed by personnel located in a U.S. branch or office to the clearing and trade execution requirements. Non-U.S. entities that are

[439] Because we have not yet issued any clearing determinations, no security-based swaps are currently subject to mandatory clearing. See Section II.B.3, supra.

required to determine whether a transaction must be included in their dealer de minimis threshold calculations, or whether they are subject to the external business conduct rules or Regulation SBSR would be able to use the same assessment in determining whether such a transaction would be subject to the clearing and trade execution requirements. Further, transactions that were arranged, negotiated, or executed by non-U.S. persons using personnel located in a U.S. branch or office would be subject to clearing and trade execution requirements identical to those faced by U.S. persons and counterparties to U.S. persons. Such consistency in regulatory treatment could reduce competitive disparities between U.S. persons and non-U.S. persons that operate in the United States. This alternative may reduce the likelihood that a two-tier security-based swap market emerges as a result of differences in regulatory requirements across jurisdictions.

However, we preliminarily believe that this policy choice would adversely affect efficiency and increase the risk of market fragmentation. We preliminarily believe that imposing the clearing and execution requirements may impose unnecessary costs on certain non-U.S. market participants in relation to the risks posed by their activity to the United States. For example, these requirements may require non-U.S. persons and their agents to form new relationships with clearing agencies and trading platforms in the United States. Given that the risk to the U.S. financial system in the security-based swap transactions at issue in this release resides with non-U.S. persons with no recourse guarantee against U.S. persons, we preliminarily believe that any potential risk posed to the U.S. financial system does not warrant imposing clearing and trade execution requirements on these security-based swap transactions. In particular, we preliminarily believe that the margin requirements for foreign security-based swap dealers, which we have proposed to apply on an entity-level basis, would be sufficient to address

the risk to the U.S. from non-U.S. persons with no recourse guarantee against U.S. persons and that the costs of the margin requirement would be commensurate to the risks involved.

VII. Paperwork Reduction Act

A. Introduction

Certain provisions of our proposal contain "collection of information"[440] requirements within the meaning of the Paperwork Reduction Act of 1955 ("PRA") and we are submitting the proposed collections of information to the Office of Management and Budget ("OMB") for review in accordance with 44 U.S.C. 3507 and 5 CFR 1320.11. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid OMB control number.

We are proposing amendments to previously adopted Regulation SBSR, which contained 12 collections of information.[441] The proposed amendments amend the "reporting hierarchy" adopted in Regulation SBSR that specifies the side that has the duty to report a security-based swap that is a "covered transaction"[442] and provides for public dissemination of security-based swap transaction information (except as provided in rule 902(c)) for certain transactions.[443] As provided in the Regulation SBSR Adopting Release, registered SDRs are required to establish and maintain certain policies and procedures regarding how transaction data are reported and

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440 44 U.S.C. 3502(3).

441 See SBSR Adopting Release, 80 FR 14673.

442 See Regulation SBSR Adopting Release, 14567, (describing "covered transaction" as "all security-based swaps except: (1) clearing transactions; (2) security-based swaps that are executed on a platform and that will be submitted to clearing; (3) transactions where there is no U.S. person, registered security-based swap dealer, or registered major security-based swap participant on either side; and (4) transactions where there is no registered security-based swap dealer or registered major security-based swap participant on either side and there is a U.S. person on only one side").

443 See proposed rules 908(a)(1)(iii), (iv) and (v).

disseminated, and participants of registered SDRs that are registered security-based swap dealers or registered major security-based swap participants are required to establish and maintain policies and procedures that are reasonably designed to ensure that they comply with applicable reporting obligations.

The hours and costs associated with complying with Regulation SBSR constitute reporting and cost burdens imposed by each collection of information. We preliminarily believe that the methodology used for calculating the paperwork burdens set forth in the Regulation SBSR Adopting Release is appropriate for calculating the paperwork burdens associated with the amendments proposed here.

The proposed amendments containing these specific collections of information are discussed further below.

B. Reporting Obligations—Rule 901

Rule 901 sets forth various requirements relating to the reporting of covered transactions. The title of this collection is "Rule 901—Reporting Obligations."

1. Summary of collection of information

Title VII of the Dodd-Frank Act amended the Exchange Act to require the reporting of security-based swap transactions. Accordingly, we adopted rule 901 of Regulation SBSR under the Exchange Act to implement this requirement. Rule 901 specifies, with respect to each reportable event pertaining to covered transactions, who is required to report, what data must be reported, when it must be reported, where it must be reported, and how it must be reported. Rule 901(a), as adopted, established a "reporting hierarchy" that specifies the side that has the duty to report a security-based swap that is a covered transaction.[444] The reporting side, as determined

[444] See Regulation SBSR Adopting Release, 80 FR 14674 (citing notes 11-12).

by the reporting hierarchy, is required to submit the information required by Regulation SBSR to a registered SDR. The reporting side may select the registered SDR to which it makes the required report. Pursuant to rule 901(b), as adopted, if there is no registered SDR that will accept the report required by rule 901(a), the person required to make the report must report the transaction to the Commission. Rule 901(c) sets forth the primary trade information and rule 901(d) sets forth the secondary trade information that must be reported. Under the final rules, covered transactions—regardless of their notional amount—must be reported to a registered SDR at any point up to 24 hours after the time of execution, or, in the case of a security-based swap that is subject to regulatory reporting and public dissemination solely by operation of rule 908(a)(1)(ii), within 24 hours after the time of acceptance for clearing.[445] Except as required by rule 902(c), the information reported pursuant to rule 901(c) must be publicly disseminated. Information reported pursuant to rule 901(d) is for regulatory purposes only and will not be publicly disseminated.

Rule 901(e) requires the reporting of life cycle events, and adjustments due to life cycle events, within 24 hours of the time of occurrence, to the entity to which the original transaction was reported. Reports of life cycle events must contain the transaction ID of the original transaction.

In addition to assigning reporting duties, rule 901 also imposes certain duties on a registered SDR that receives security-based swap transaction data. Rule 901(f) requires a

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[445] See Regulation SBSR Adopting Release, Section VII(B)(1) (discussing rule 901(j) and the rationale for 24-hour reporting timeframe). Rule 901(j) provides that, if 24 hours after the time of execution would fall on a non-business day (i.e., a Saturday, Sunday, or U.S. federal holiday), reporting is required by the same time on the next business day. Rule 908(a)(1)(ii), as adopted, provides that a security-based swap that is subject to regulatory reporting and public dissemination solely by operation of rule 908(a)(1)(ii)—i.e., because the security-based swap has been accepted for clearing by a clearing agency having its principal place of business in the United States—must be reported within 24 hours of acceptance for clearing.

registered SDR to timestamp, to the second, any information submitted to it pursuant to rule 901, and rule 901(g) requires a registered SDR to assign a transaction ID to each security-based swap, or establish or endorse a methodology for transaction IDs to be assigned by third parties. Rule 901(h) requires that all information required by rule 901 be transmitted electronically in a format required by the registered SDR.

Rule 901(i) requires reporting of pre-enactment security-based swaps and transitional security-based swaps to the extent that information about such transactions is available.

2. Use of information

The security-based swap transaction information required to be reported pursuant to rule 901 will be used by registered SDRs, market participants, the Commission, and other relevant authorities. The information reported pursuant to rule 901 will be used by registered SDRs to publicly disseminate reports of security-based swap transactions, as well as to offer a resource for us and other relevant authorities to obtain detailed information about the security-based swap market. Market participants will use the public market data feed, among other things, to assess the current market for security-based swaps and to assist in the valuation of their own positions. We and other relevant authorities will use information about security-based swap transactions reported to and held by registered SDRs to monitor and assess systemic risks, as well as for market surveillance purposes.

3. Respondents

Rule 901(a) assigns reporting duties for covered transactions. In the Regulation SBSR Adopting Release we maintained our preliminary estimate of 300 respondents.[446] Based on an

[446] See Regulation SBSR Adopting Release, 80 FR 14674; Cross-Border Proposing Release, 78 FR 31113 (lowering estimate of respondents from 1,000 to 300).

analysis of the TIW data, we estimate that the proposed amendments set forth in this release would result in an additional 120 respondents that would be required to report transactions under the proposed amendments to Regulation SBSR that are not already required to report under the Regulation SBSR as adopted. Per estimates discussed above regarding the programmatic costs and benefits of regulatory reporting and public dissemination, we estimated that these 120 new respondents will be made up of 90 persons and approximately 30 other persons that are registered broker-dealers (including registered SB SEFs).[447]

4. Total initial and annual reporting and recordkeeping burdens of rule 901 of Regulation SBSR

Pursuant to rule 901, covered transactions must be reported to a registered SDR or to the Commission. Together, sections (a), (b), (c), (d), (e), (h), and (j) of rule 901 set forth the parameters that govern how covered transactions are reported. Rule 901(i) addresses the reporting of pre-enactment and transitional security-based swaps. These reporting requirements impose initial and ongoing burdens on respondents. We preliminarily believe that these burdens would be a function of, among other things, the number of reportable events and the data elements required to be reported for each such event. Rule 901(f) requires a registered SDR to time stamp, to the second, all reported information, and rule 901(g) requires a registered SDR to assign a transaction ID to each security-based swap, or establish or endorse a methodology for transaction IDs to be assigned by third parties. These requirements impose initial and ongoing burdens on registered SDRs. We preliminarily believe that the proposed amendments addressed in this release would not impact the cost burdens resulting from rules 901(f) and 901(g) on

[447] See section VI.B.3 and n.403, supra.

registered SDRs because the number of respondents does not impact our calculation of these costs.[448] Therefore we do not address the costs associated with these provisions.

For Respondents. The reporting hierarchy set forth in rule 901(a) is designed to place the duty to report covered transactions on counterparties who are most likely to have the resources and who are best able to support the reporting function.

Respondents that fall under the reporting hierarchy in rule 901(a)(2)(ii) incur certain burdens as a result thereof with respect to their reporting of covered transactions. As stated above, we preliminarily believe that an estimate of 120 additional respondents that would incur the duty to report under Regulation SBSR is reasonable for estimating collection of information burdens. This estimate includes all persons that would incur a reporting duty under proposed amendments to Regulation SBSR, that are not already subject to burdens under current rule 901.

In the Regulation SBSR Adopting Release, we estimated that there were likely to be approximately 3 million reportable events per year under rule 901.[449] We further estimated that approximately 2 million of these reportable events would consist of uncleared transactions. We estimated that 2 million of the 3 million total reportable events would consist of the initial reporting of security-based swaps as well as the reporting of any life cycle events. We also estimated that of the 2 million reportable events, approximately 900,000 would involve the reporting of new security-based swap transactions, and approximately 1,100,000 would involve the reporting of life cycle events under rule 901(e).

Based on our assessment of the effect of the proposed amendments to Regulation SBSR, we estimate that they would result in approximately 2,700 additional reportable events per year

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448 See Regulation SBSR Adopting Release, 80 FR 14676-77.

449 See Regulation SBSR Adopting Release, 80 FR 14675.

under rule 901. Taking a similar approach to the Regulation SBSR Adopting Release but also accounting for security-based swaps that would be reported by a registered broker-dealer, we estimate that, of the 2,700 new reportable events, 1,512 would involve the reporting of new security-based swap transactions, and approximately 1,188 would involve the reporting of life cycle events under rule 901(e).[450] Based on these estimates, we preliminarily believe that rule 901(a) would result in respondents having a total burden of 7.6 hours attributable to the initial reporting of security-based swaps by respondents to registered SDRs under rules 901(c) and 901(d) over the course of a year.[451] We further estimate that respondents would have a total burden of 5.9 hours attributable to the reporting of life cycle events under rule 901(e) over the course of a year.[452] Therefore, we preliminarily believe that the proposed amendments to Regulation SBSR would result in a total reporting burden for respondents under rules 901(c) and 901(d) along with the reporting of life cycle events under rule 901(e) of 13.5 burden hours per year. We continue to believe that many reportable events would be reported through electronic means and that the ratio of electronic reporting to manual reporting is likely to increase over

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450 As noted above, we expect that 20% of the new reportable events would be reported by registered broker-dealers pursuant to 901(a)(2)(ii)(E)(4) and thus would involve the reporting only of new security-based swap transactions and not of life-cycle events. See note 403, supra. Under this assumption, we would expect 540 reportable events (2,700 * 0.2) to be new security-based swap transactions reported by registered broker-dealers, and 972 reportable events to be other new security-based swap transactions that would be required to be reported under the proposed rule ((2,700 - 540) * 0.45), for a total of 1,512 reportable events that are new security-based swap transactions. The remaining 1,188 reportable events ((2,700 - 540) * 0.55) would be life-cycle events reportable under rule 901(e). Cf. Regulation SBSR Adopting Release, 80 FR 14676.

451 In the Regulation SBSR Proposing Release, we estimated that it would take approximately 0.005 hours for each security-based swap transaction to be reported. See 75 FR at 75249 n.195. We calculate the following: ((1,512* 0.005) / (120 respondents)) = 0.06 burden hours per respondent or 7.6 total burden hours attributable to the initial reporting of security-based swaps.

452 In the Regulation SBSR Proposing Release, we estimated that it would take approximately 0.005 hours for each security-based swap transaction to be reported. See 75 FR at 75249 n.195. We calculate the following: ((1,188 * 0.005) / (120 respondents)) = 0.05 burden hours per reporting side or 5.9 total burden hours attributable to the reporting of life cycle events under rule 901(e).

time. We continue to believe that the bulk of the burden hours estimated above would be attributable to manually reported transactions.[453] Thus, respondents that capture and report transactions electronically would likely incur fewer burden hours than those respondents that capture and report transactions manually.

Based on the foregoing and applying the same calculation methods used in the Regulation SBSR Adopting Release, we estimate that rule 901, as proposed in this release, would impose an estimated total first-year burden of approximately 1,361 hours[454] per respondent for a total first-year burden of 163,320 hours for all respondents that would incur the duty to report under the proposed amendments to rule 901(a)(2)(ii)(E).[455] We estimate that rule 901, when applied to new respondents resulting from the proposed amendments to rule 901(a), would impose ongoing annualized aggregate burdens of approximately 654 hours[456] per respondent for a total aggregate annualized burden of 78,480 hours for all new respondents.[457] We further estimate that rule 901 would impose initial and ongoing annualized dollar cost

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453 See Regulation SBSR Adopting Release, 80 FR 14676.

454 We derived our estimate from the following: (355 hours (one-time hourly burden for establishing an OMS) + 172 hours (one-time hourly burden for establishing security-based swap reporting mechanisms) + 180 hours (one-time hourly burden for compliance and ongoing support) = 707 hours (one-time total hourly burden). See Regulation SBSR Proposing Release, 75 FR 75248-50 nn.186, 194, and 201. (436 hours (annual-ongoing hourly burden for internal order management) + 0.11 hours (revised annual-ongoing hourly burden for security-based swap reporting mechanisms) + 218 hours (annual-ongoing hourly burden for compliance and ongoing support) = 654 hours (one-time total hourly burden. See id. 75248-50 nn.187 and 201 (707 one-time hourly burden + 654 revised annual-ongoing hourly burden = 1,361 total first-year hourly burden).

455 We derived our estimate from the following: (1,361 hours per respondent * 120 respondents) = 163,320 hours.

456 See Regulation SBSR Adopting Release, 80 FR 14676 (citing Cross-Border Adopting Release, 78 FR 31112-15).

457 We derived our estimate from the following: (654 hours per respondent * 120 respondents) = 78,480 hours.

burdens of $201,000 per respondent, for total aggregate initial and ongoing annualized dollar cost burdens of $24,120,000.[458]

C. Correction of Errors in Security-Based Swap Information—Rule 905

Rule 905, as adopted, establishes procedures for correcting errors in reported and disseminated security-based swap information. The title of this collection is "Rule 905—Correction of Errors in Security-Based Swap Information."

1. Summary of collection of information

Rule 905 establishes duties for security-based swap counterparties and registered SDRs to correct errors in information that previously has been reported.

Counterparty Reporting Error. Under rule 905(a)(1), where a side that was not the respondent for a security-based swap transaction discovers an error in the information reported with respect to such security-based swap, the counterparty must promptly notify the respondent of the error. Under rule 905(a)(2), where a respondent for a security-based swap transaction discovers an error in the information reported with respect to a security-based swap, or receives notification from its counterparty of an error, the respondent must promptly submit to the entity to which the security-based swap was originally reported an amended report pertaining to the original transaction. The amended report must be submitted to the registered SDR in a manner consistent with the policies and procedures of the registered SDR required pursuant to rule 907(a)(3).

Duty of Registered SDR to Correct. Rule 905(b) sets forth the duties of a registered SDR relating to corrections. If the registered SDR either discovers an error in a transaction on its system or receives notice of an error from a respondent, rule 905(b)(1) requires the registered

[458] See Regulation SBSR Adopting Release, 80 FR 14676 nn.1066 and 1078. We derived our estimate from the following: ($201,000 per respondent * 120 respondents) = $24,120,000.

SDR to verify the accuracy of the terms of the security-based swap and, following such verification, promptly correct the erroneous information contained in its system. Rule 905(b)(2) further requires that, if such erroneous information relates to a security-based swap that the registered SDR previously disseminated and falls into any of the categories of information enumerated in rule 901(c), the registered SDR must publicly disseminate a corrected transaction report of the security-based swap promptly following verification of the trade by the counterparties to the security-based swap, with an indication that the report relates to a previously disseminated transaction.

2. Use of information

The security-based swap transaction information required to be reported pursuant to rule 905 will be used by registered SDRs, participants of those SDRs, the Commission, and other relevant authorities. Participants will be able to use such information to evaluate and manage their own risk positions and satisfy their duties to report corrected information to a registered SDR. A registered SDR will need the required information to correct security-based swap transaction records, in order to maintain an accurate record of a participant's positions as well as to disseminate corrected information. The Commission and other relevant authorities will need the corrected information to have an accurate understanding of the market for surveillance and oversight purposes.

3. Respondents

Rule 905 applies to all participants of registered SDRs. As noted above, we estimated that there would be approximately 300 respondents that incur the duty to report security-based swap transactions pursuant to current rule 901. As noted above, we preliminarily estimate that an additional 120 respondents would incur the duty to report under the proposed amendments to Regulation SBSR. Because any of these additional participants could become aware of errors in

their reported transaction data, we estimate that there may be 120 respondents for purposes of the proposed amendments.

4. Total initial and annual reporting and recordkeeping burdens

The duty to promptly submit amended transaction reports to the appropriate registered SDR after discovery of an error, as required under rule 905(a)(2), will impose burdens on respondents. The duty to promptly notify the relevant respondent after discovery of an error, as required under rule 905(a)(1), will impose burdens on non-reporting participants.

With respect to respondents, we preliminarily believe that rule 905(a) will impose an initial, one-time burden associated with designing and building the respondent's reporting system to be capable of submitting amended security-based swap transactions to a registered SDR. We continue to believe that designing and building appropriate reporting system functionality to comply with rule 905(a)(2) would be a component of, and represent an incremental "add-on" to, the cost to build a reporting system and develop a compliance function as required under existing rule 901. Based on discussions with industry participants, we previously estimated this incremental burden to be equal to 5% of the one-time and annual burdens associated with designing and building a reporting system that is in compliance with rule 901, plus 10% of the corresponding one-time and annual burdens associated with developing the respondent's overall compliance program required under rule 901.[459] This estimate was based on similar calculations contained in the Regulation SBSR Proposing Release,[460] updated to reflect new estimates relating to the number of reportable events and the number of entities with reporting duties. Taking a similar approach with respect to the proposed amendments to Regulation SBSR, we

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459 See Regulation SBSR Adopting Release, 80 FR 14682.

460 See Regulation SBSR Proposing Release, 75 FR 75254.

estimate that the new respondents would incur, as a result of rule 905(a), an initial (first-year) aggregate burden of 5,808.7 hours, which is 48.4 burden hours per respondent,[461] and an ongoing aggregate annualized burden of 2,616.7 hours, which is 21.8 burden hours per respondent.[462]

We preliminarily believe that the actual submission of amended transaction reports required under rule 905(a)(2) would not result in a material burden because this would be done electronically though the reporting system that the respondent must develop and maintain to comply with rule 901. The overall burdens associated with such a reporting system are addressed in our analysis of rule 901.[463]

D. Policies and Procedures for Registered Broker-Dealers—Rule 906(c)

1. Summary of collection of information

The proposed amendments to rule 906(c) would require each participant that is a registered broker-dealer that becomes a participant solely as a result of making a report to satisfy an obligation under proposed rule 901(a)(2)(ii)(E)(4) to establish, maintain, and enforce written policies and procedures that are reasonably designed to ensure compliance with applicable security-based swap transaction reporting obligations. Each such participant also would be required to review and update its policies and procedures at least annually.

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461 This figure is calculated as follows: [(((172 burden hours for one-time development of reporting system) x (0.05)) + ((0.11 burden hours annual maintenance of reporting system) x (0.05)) + ((180 burden hours one-time compliance program development) x (0.1)) + ((218 burden hours annual support of compliance program) x (0.1))) x (120 respondents)] = 5,808.7 burden hours, which is 48.4 burden hours per respondent.

462 This figure is calculated as follows: [(((0.11 burden hours annual maintenance of reporting system) x (0.05)) + ((218 burden hours annual support of compliance program) x (0.1))) x (120 respondents)] = 2,616.7 burden hours, which is 21.8 burden hours per respondent.

463 See Section VII.B, supra.

2. Use of information

The policies and procedures required under the proposed amendments to rule 906(c) would be used by participants to aid in their compliance with Regulation SBSR, and also used by the Commission as part of its ongoing efforts to monitor and enforce compliance with the federal securities laws, including Regulation SBSR, through, among other things, examinations and inspections.

3. Respondents

The proposed amendments to rule 906(c) would result in the rule applying to registered broker-dealers that are likely to become participants solely as a result of making a report to satisfy an obligation under proposed rule 901(a)(2)(ii)(E)(4). The Commission estimates that there would be 30 such registered broker-dealers.

4. Total initial and annual reporting and recordkeeping burdens

The proposed amendment to rule 906(c) would require each registered broker-dealer that is likely to become a participant solely as a result of making a report to satisfy an obligation under proposed rule 901(a)(2)(ii)(E)(4) to establish, maintain, and enforce written policies and procedures that are reasonably designed to ensure compliance with applicable security-based swap transaction reporting obligations. The proposed amendment to rule 906(c) also would require each such registered broker-dealer to review and update such policies and procedures at least annually. We estimate that the one-time, initial burden for each such registered broker-dealer to adopt written policies and procedures as required under the proposed amendments to rule 906(c) would be similar to the rule 906(c) burdens discussed in the Regulation SBSR Adopting Release for covered participants, and would be approximately 216 burden hours per

registered broker-dealer.[464] As discussed in the Regulation SBSR Adopting Release,[465] this figure is based on the estimated number of hours to develop a set of written policies and procedures, program systems, implement controls and oversight, train relevant employees, and perform necessary testing. In addition, we estimate the burden of maintaining such policies and procedures, including a full review at least annually would be approximately 120 burden hours for each registered broker-dealer that is likely to become a participant solely as a result of making a report to satisfy an obligation under proposed rule 901(a)(2)(ii)(E)(4).[466] This figure includes an estimate of hours related to reviewing existing policies and procedures, making necessary updates, conducting ongoing training, maintaining controls systems, and performing necessary testing. Accordingly, the Commission estimates that the initial aggregate annualized burden associated with the proposed amendments to rule 906(c) would be 10,080 burden hours, which corresponds to 336 burden hours per registered broker-dealer that is likely to become a participant solely as a result of making a report to satisfy an obligation under proposed rule 901(a)(2)(ii)(E)(4).[467] The Commission estimates that the ongoing aggregate annualized burden associated with the proposed amendments to rule 906(c) would be 3,600 burden hours, which

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464 See Regulation SBSR Adopting Release, 80 FR 14684. This figure is based on the following: [(Sr. Programmer at 40 hours) + (Compliance Manager at 40 hours) + (Compliance Attorney at 40 hours) + (Compliance Clerk at 40 hours) + (Sr. Systems Analyst at 32 hours) + (Director of Compliance at 24 hours)] = 216 burden hours per registered broker-dealer that is likely to become a participant solely as a result of making a report to satisfy an obligation under proposed rule 901(a)(2)(ii)(E)(4).

465 See id.

466 See id. This figure is based on the following: [(Sr. Programmer at 8 hours) + (Compliance Manager at 24 hours) + (Compliance Attorney at 24 hours) + (Compliance Clerk at 24 hours) + (Sr. Systems Analyst at 16 hours) + (Director of Compliance at 24 hours)] = 120 burden hours per registered clearing agency or platform.

467 This figure is based on the following: [(216 + 120 burden hours) x (30 registered broker-dealers that are likely to become a participant solely as a result of making a report to satisfy an obligation under proposed rule 901(a)(2)(ii)(E)(4))] = 10,080 burden hours.

corresponds to 120 burden hours per registered broker-dealer that is likely to become a participant solely as a result of making a report to satisfy an obligation under proposed rule 901(a)(2)(ii)(E)(4).[468]

E. Collection of Information is Mandatory

Each collection of information discussed above is mandatory.

F. Confidentiality of Responses to Collection of Information

Information collected pursuant to rule 905 would be widely available to the extent that it corrects information previously reported pursuant to rule 901(c) and incorporated into security-based swap transaction reports that are publicly disseminated by a registered SDR pursuant to rule 902. Most of the information required under rule 902 would be widely available to the public to the extent it is incorporated into security-based swap transaction reports that are publicly disseminated by a registered SDR pursuant to rule 902. However, rule 902(c) prohibits public dissemination of certain kinds of transactions and certain kinds of transaction information. An SDR, pursuant to section 13(n)(5) of the Exchange Act and rules 13n-4(b)(8) and 13n-9 thereunder is required to maintain the privacy of this security-based swap information. To the extent that we receive confidential information pursuant to this collection of information, we anticipate that we will keep such information confidential, subject to the provisions of applicable law. The proposed amendments to rule 906(c) would require certain registered broker-dealers to establish, maintain, and enforce certain written policies and procedures. The collection of information required by rule 906(c) would not be widely available. To the extent that the

[468] This figure is based on the following: [(120 burden hours) x (30 registered broker-dealers that are likely to become a participant solely as a result of making a report to satisfy an obligation under proposed rule 901(a)(2)(ii)(E)(4))] = 3,600 burden hours.

Commission receives confidential information pursuant to this collection of information, we anticipate that we would keep such information confidential, subject to applicable law.

G. Request for comment

Pursuant to 44 U.S.C. 3506(c)(2)(B), the Commission solicits comment to:

- Evaluate whether the proposed collection of information is necessary for the proper performance of our functions, including whether the information shall have practical utility;
- Evaluate the accuracy of our estimate of the burden of the proposed collection of information;

  Determine whether there are ways to enhance the quality, utility, and clarity of the information to be collected; and
- Evaluate whether there are ways to minimize the burden of collection of information on those who are to respond, including through the use of automated collection techniques or other forms of information technology.

Persons submitting comments on the collection of information requirements should direct them to the Office of Management and Budget, Attention: Desk Officer for the Securities and Exchange Commission, Office of Information and Regulatory Affairs, Washington, DC 20503, and should also send a copy of their comments to Brent J. Fields, Secretary, Securities and Exchange Commission, 100 F Street NE, Washington, DC 20549-1090, with reference to File Number S7-06-15. Requests for materials submitted to OMB by the Commission with regard to this collection of information should be in writing, with reference to File Number S7-06-15 and be submitted to the Securities and Exchange Commission, Office of FOIA/PA Services, 100 F Street NE., Washington, DC 20549-2736. As OMB is required to make a decision concerning

the collections of information between 30 and 60 days after publication, a comment to OMB is best assured of having its full effect if OMB receives it within 30 days of publication.

VIII. Consideration of Impact on the Economy

For purposes of the Small Business Regulatory Enforcement Fairness Act of 1996 ("SBREFA")[469] the Commission requests comment on the potential effect of these proposed amendments on the United States economy on an annual basis. The Commission also requests comment on any potential increases in costs or prices for consumers or individual industries, and any potential effect on competition, investment, or innovation. Commenters are requested to provide empirical data and other factual support for their views to the extent possible.

IX. Regulatory Flexibility Act Certification

A. Certification for Proposed Rule and Proposed Amendments to Exchange Act Rules 3a71-3 and 3a71-5

Section 3(a) of the Regulatory Flexibility Act of 1980 ("RFA")[470] requires the Commission to undertake an initial regulatory flexibility analysis of the impact of the proposed rule amendments on small entities unless the Commission certifies that the rule, if adopted, would not have a significant impact on a substantial number of "small entities."[471]

For purposes of Commission rulemaking in connection with the RFA,[472] a small entity includes: (1) when used with reference to an "issuer" or a "person," other than an investment

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469 Public Law 104–121, Title II, 110 Stat. 857 (1996) (codified in various sections of 5 U.S.C., 15 U.S.C. and as a note to 5 U.S.C. 601).

470 5 U.S.C. 603(a).

471 5 U.S.C. 605(b)

472 Although section 601(b) of the RFA defines the term "small entity," the statute permits agencies to formulate their own definitions. The Commission has adopted definitions for the term "small entity" for the purposes of Commission rulemaking in accordance with the RFA. Those definitions, as relevant to this proposed rulemaking, are set forth in Rule 0-10 under the Exchange Act, 17 CFR 240.0-10. See Exchange Act Release No. 18451 (January, 28, 1982), 47 FR 5215 (February, 4, 1982) (File No. AS-305).

company, an "issuer" or "person" that, on the last day of its most recent fiscal year, had total assets of $5 million or less;[473] or (2) a broker-dealer with total capital (net worth plus subordinated liabilities) of less than $500,000 on the date in the prior fiscal year as of which its audited financial statements were prepared pursuant to Rule 17a-5(d) under the Exchange Act,[474] or, if not required to file such statements, a broker-dealer with total capital (net worth plus subordinated liabilities) of less than $500,000 on the last day of the preceding fiscal year (or in the time that it has been in business, if shorter); and is not affiliated with any person (other than a natural person) that is not a small business or small organization.[475] Under the standards adopted by the Small Business Administration, small entities in the finance and insurance industry include the following: (i) for entities engaged in credit intermediation and related activities, entities with $175 million or less in assets;[476] (ii) for entities engaged in non-depository credit intermediation and certain other activities, entities with $7 million or less in annual receipts;[477] (iii) for entities engaged in financial investments and related activities, entities with $7 million or less in annual receipts;[478] (iv) for insurance carriers and entities engaged in related activities, entities with $7 million or less in annual receipts;[479] and (v) for funds, trusts, and other financial vehicles, entities with $7 million or less in annual receipts.[480]

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473 See 17 CFR 240.0-10(a).

474 See 17 CFR 240.17a-5(d).

475 See 17 CFR 240.0-10(c).

476 See 13 CFR 121.201 (Subsector 522).

477 See id. at Subsector 522.

478 See id. at Subsector 523.

479 See id. at Subsector 524.

480 See id. at Subsector 525.

As we stated in the Cross-Border Adopting Release, we continue to believe that the types of entities that would engage in more than a de minimis amount of dealing activity involving security-based swaps would not be "small entities" for purposes of the RFA.[481] Based on feedback from market participants and our information about the security-based swap markets, we believe that firms that are likely to engage in security-based swap dealing activity at levels that may lead them to perform de minimis calculations under the "security-based swap dealer" definition are large financial institutions that exceed the thresholds defining "small entities" as set forth above. Accordingly, the Commission preliminarily believes that it is unlikely that the proposed amendments regarding the registration of security-based swap dealers would have a significant economic impact on a substantial number of small entities.

For the foregoing reasons, the Commission certifies that the proposed rule and amendments to Exchange Act 3a71-3 and 3a71-5 would not have a significant economic impact on a substantial number of small entities for purposes of the RFA. We encourage written comments regarding this certification. We request that commenters describe the nature of any impact on small entities and provide empirical data to illustrate the extent of the impact.

B. Initial Regulatory Flexibility Analysis for Proposed Amendments to Regulation SBSR

The Commission has prepared this Initial Regulatory Flexibility Act Analysis in accordance with 5 U.S.C. 603. This initial Regulatory Flexibility Act Analysis relates to the proposed amendments to Regulation SBSR under the Exchange Act, specifically rules 900, 901, 906, 907, and 908 under the Exchange Act.

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481 See Cross-Border Adopting Release, 79 FR 47368.

1. Reasons for, and Objectives of, the Proposed Action and Legal Basis

The primary reason for, and objective of, the proposed amendments to Regulation SBSR is to address the application of the regulatory reporting and public dissemination requirements to certain transactions not addressed in the Regulation SBSR Adopting Release or the Regulation SBSR Proposed Amendments Release and to incorporate our revised approach to transactions of non-U.S. persons who are engaged in dealing activity from a location in the United States into Regulation SBSR. Pursuant to Exchange Act sections 13A(a)(1), 13(m)(1)(G), 13(m)(1)(B)-(D), and 13(n)(5)(D)(ii), the Commission is proposing amendments to Regulation SBSR regarding the reporting and public dissemination of certain security-based swap transactions.[482]

Proposed rule 908(a)(1)(v) would require a security-based swap transaction connected with a non-U.S. person's security-based swap dealing activity that is arranged, negotiated, or executed by personnel of such non-U.S. person located in a U.S. branch or office, or by personnel of such non-U.S. person's agent located in a U.S. branch or office, to be reported to a registered SDR and publicly disseminated. Requiring these transactions to be reported to a registered SDR should enhance our ability to oversee relevant activity related to security-based swap dealing occurring within the United States as well as our ability to monitor market participants for compliance with specific Title VII requirements.[483] It should also improve our ability to monitor for manipulative and abusive practices involving security-based swap transactions or transactions in related underlying assets, such as corporate bonds or other securities transactions that result from dealing activity, or other relevant activity, in the U.S.

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482 See Section V.E, supra.

483 See section V.E.2(a), supra.

market.[484] Subjecting these transactions to the public dissemination requirements of Regulation SBSR should enhance the level of transparency in the U.S. security-based swap market, potentially reducing implicit transaction costs and promoting greater price efficiency.[485] Ensuring that post-trade information encompasses transactions involving a non-U.S. person that arranged, negotiated, or executed the security-based swap in connection with its dealing activity using personnel (personnel of an agent) located in a U.S. branch or office, could increase price competition and price efficiency in the security-based swap market and should enable all market participants to have more comprehensive information with which to make trading and valuation determinations.[486]

Proposed rule 908(a)(1)(iii) would require a security-based swap transaction that is executed on a platform having its principal place of business in the United States to be reported to a registered SDR and publicly disseminated pursuant to Regulation SBSR. Requiring these security-based swaps to be reported to a registered SDR would permit the Commission and other relevant authorities to observe, in a registered SDR, all transactions executed on such a platform and to carry out oversight of such security-based swaps. Furthermore, we preliminarily believe that public dissemination of such transactions would have value to participants in the U.S. security-based swap market, who are likely to trade the same or similar products, as these products would have been listed by a platform having its principal place of business in the United States.[487]

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484 Id.

485 See id. and note 325, supra.

486 See section V.E.2(a), supra.

487 See section V.E.2(b), supra.

Proposed rule 908(a)(1)(iv) would require a security-based swap transaction that is effected by or through a registered broker-dealer (including a registered SB SEF) to be reported to a registered SDR and publicly disseminated pursuant to Regulation SBSR. Under proposed rule 908(a)(2)(ii)(E)(4), the registered broker-dealer would be required to report the transaction if neither side includes a U.S. person, a registered security-based swap dealer, a registered major security-based swap participant, or a non-U.S. person who arranged, negotiated, or executed the security-based swap from a location in the United States. Registered broker-dealers play a key role as intermediaries in the U.S. financial markets. To improve integrity and transparency in those markets, we believe that it is important that the Commission, and other relevant authorities, have ready access to detailed information about the security-based swap transactions that such persons intermediate. Furthermore, we preliminarily believe that public dissemination of such transactions would have value to participants in the U.S. security-based swap market, who are likely to trade the same or similar products.[488]

2. Small Entities Subject to the Proposed Rules

For purposes of Commission rulemaking in connection with the RFA, a small entity includes: (1) when used with reference to an "issuer" or a "person," other than an investment company, an "issuer" or "person" that, on the last day of its most recent fiscal year, had total assets of $5 million or less;[489] or (2) a broker-dealer with total capital (net worth plus subordinated liabilities) of less than $500,000 on the date in the prior fiscal year as of which its audited financial statements were prepared pursuant to Exchange Act rule 17a-5(d),[490] or, if not required to file such statements, a broker-dealer with total capital (net worth plus subordinated

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488 See section V.E.2(c), supra.

489 See 17 CFR 240.0-10(a).

490 See 17 CFR 240.17a-5(d).

liabilities) of less than $500,000 on the last day of the preceding fiscal year (or in the time that it has been in business, if shorter); and is not affiliated with any person (other than a natural person) that is not a small business or small organization.[491] Under the standards adopted by the Small Business Administration, small entities in the finance and insurance industry include the following: (i) for entities engaged in credit intermediation and related activities, entities with $175 million or less in assets;[492] (ii) for entities engaged in non-depository credit intermediation and certain other activities, entities with $7 million or less in annual receipts;[493] (iii) for entities engaged in financial investments and related activities, entities with $7 million or less in annual receipts;[494] (iv) for insurance carriers and entities engaged in related activities, entities with $7 million or less in annual receipts;[495] and (v) for funds, trusts, and other financial vehicles, entities with $7 million or less in annual receipts.[496]

As noted in the Regulation SBSR Proposed Amendments Release, we believe, based on input from security-based swap market participants, that the majority of security-based swap transactions have at least one counterparty that is either a security-based swap dealer or major security-based swap participant, and that these entities—whether registered broker-dealers or not—would exceed the thresholds defining "small entities" set out above.[497] For this reason, we continue to believe that the majority of proposed amendments to Regulation SBSR would not

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491 See 17 CFR 240.0-10(c).

492 See 13 CFR 121.201 (Subsector 522).

493 See id. at Subsector 522.

494 See id. at Subsector 523.

495 See id. at Subsector 524.

496 See id. at Subsector 525.

497 See Regulation SBSR Proposed Amendments Release, 80 FR 14801. See also Regulation SBSR Adopting Release, 80 FR 14727-28.

have a significant economic impact on a substantial number of small entities for purposes of the RFA. However, the proposed amendments would require registered broker-dealers (including a registered SB SEF) to report a security-based swap transaction that is effected by or through it. As noted above, we estimate that 30 registered broker-dealers (including registered SB SEFs) may be required to report such transactions,[498] though we are not able to estimate the number of these registered broker-dealers that would be "small entities." Given the nature of the security-based swap market, we preliminarily believe that it is unlikely that these registered broker-dealers would be small entities, though we request comment on the number of registered broker-dealers that are small entities that would be impacted by our proposed amendments, including any available empirical data.

3. Projected Reporting, Recordkeeping and Other Compliance Requirements

As discussed above, the proposed amendments to Regulation SBSR would require a security-based swap transaction that is effected by or through a registered broker-dealer (including a registered SB SEF) to be reported to a registered SDR by the registered broker-dealer if neither side of the security-based swap transaction includes a U.S. person, a registered security-based swap dealer, a registered major security-based swap participant, or a non-U.S. person who arranged, negotiated, or executed the security-based swap from a location in the United States. We preliminarily believe, as discussed above, that registered broker-dealers (including registered SB SEFs) would incur certain assessment costs associated with performing an analysis of their clients (in the case of registered-broker dealers) and members (in the case of registered SB SEFs)[499] to determine whose trades they are obligated to report under the proposed

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498 See section VII.B.3, supra.

499 See section VI.A.1, supra.

rules, which would be supported by systems that would record and maintain this information over time.[500]

Additionally, under the proposed amendments to rule 906(c), these registered broker-dealers would be required to establish, maintain, and enforce policies and procedures that are reasonably designed to ensure that the registered broker-dealer complies with any obligations to report information to a registered security-based swap data repository in a manner consistent with Regulation SBSR. Further, these registered broker-dealers would be required to review these policies and procedures at least annually.[501]

4. Duplicative, Overlapping or Conflicting Federal Rules

The Commission believes there are no rules that duplicate, overlap, or conflict with the proposed amendments.

5. Significant Alternatives

Pursuant to section 3(a) of the Regulatory Flexibility Act,[502] the Commission must consider certain types of alternatives, including: (1) The establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities; (2) the clarification, consolidation or simplification of compliance and reporting requirements under the rule for small entities; (3) the use of performance rather than design standards; and (4) an exemption from coverage of the rule, or any part of the rule, for small entities.

We are proposing to require registered broker-dealers (including registered SB SEFs) to report security-based swap transactions that are effected by or through it if neither side of the

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500 Id.

501 See section VI.B.3, supra.

502 5 U.S.C. 603(c)

security-based swap transaction includes a U.S. person, a registered security-based swap dealer, a registered major security-based swap participant, or a non-U.S. person who arranged, negotiated, or executed the security-based swap from a location in the United States. The proposed amendments would enable the Commission to gain a better understanding of the security-based swap market, including the size and scope that market, and should enable us to identify exposure to risks undertaken by individual market participants or at various levels of aggregation, as well as credit exposures that arise between counterparties.[503] The regulatory data collected as a result of the proposed amendments would enable us to conduct robust monitoring of the security-based swap market for potential risks to financial stability.[504] The Commission considered whether it is necessary or appropriate to establish different compliance and reporting requirements under the rule; or clarify, consolidate, or simplify the compliance and reporting requirements for small entities under the rule. Because the proposed rule amendments would enhance the Commission's ability to oversee relevant activity related to security-based swap dealing occurring within the United States, our ability to monitor market participants for compliance with specific Title VII requirements, and our ability to monitor for manipulative and abusive practices involving security-based swap transactions, we preliminarily believe that small entities should be covered by the proposed amendments to Regulation SBSR. We preliminarily believe that establishing different compliance or reporting requirements for small entities, or exempting small entities from the proposed amendments could complicate the rules and potentially create gaps in the regulatory data that is reported and publicly disseminated that would be inconsistent with the goals of Title VII and the proposed amendments. Additionally,

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503 See Section VI.B.3, supra.

504 See Section VI.B.3, supra.

we do not consider performance rather than design standards to be consistent with the statutory mandate requiring reporting of security-based swaps to registered SDRs and the public dissemination of transaction and pricing data to enhance price discovery of security-based swaps.[505]

6. Solicitation of Comment

We are soliciting comments regarding this analysis. We request comment on the number of small entities that would be subject to the amendments and whether the proposed amendments would have any effects that have not been discussed. We request that commenters describe the nature of any effects on small entities subject to the amendments and provide empirical data to support the nature and extent of the effects.

X. Statutory Basis and Text of Proposed Rules

Pursuant to the Exchange Act, 15 U.S.C. § 78a et seq., and particularly, Sections 3(b), 23(a)(1), 3C(e), 11A(b), 13(m)(1), 13A(a), 17(a), and 30(c) thereof, Sections 712(a)(2), (6), and 761(b) of the Dodd-Frank Act, the SEC is proposing to amend rules 3a71-3 and 3a71-5, and 900, 901, 906, 907 and 908, under the Exchange Act.

List of Subjects

17 CFR Part 240

Brokers, Confidential business information, Fraud, Reporting and recordkeeping requirements, Securities.

17 CFR Part 242

Brokers, Fraud, Reporting and recordkeeping requirements, Securities.

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[505] See Exchange Act sections 13(m)(1)(G) and 13(m)(1)(B).

Text of Proposed rules

For the reasons stated in the preamble, the SEC is proposing to amend Title 17, Chapter II of the Code of the Federal Regulations as follows:

PART 240—GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE ACT OF 1934

1. The general authority citation for part 240 continues to read, and a sectional authority is added in numerical order to read as follows:

Authority: 15 U.S.C. 77c, 77d, 77g, 77j, 77s, 77z-2, 77z-3, 77eee, 77ggg, 77nnn, 77sss, 77ttt, 78c, 78c-3, 78c-5, 78d, 78e, 78f, 78g, 78i, 78j, 78j-1, 78k, 78k-1, 78*l*, 78m, 78n, 78n-1, 78o, 78o-4, 78o-10, 78p, 78q, 78q-1, 78s, 78u-5, 78w, 78x, 78*ll*, 78mm, 80a–20, 80a–23, 80a–29, 80a–37, 80b–3, 80b–4, 80b–11, and 7201 et seq., and 8302; 7 U.S.C. 2(c)(2)(E); 12 U.S.C. 5221(e)(3); 18 U.S.C. 1350; and Pub. L. 111-203, 939A, 124 Stat. 1376, (2010) unless otherwise noted.

* * * * *

Sections 3a71-3 and 3a71-5 are also issued under Pub. L. 111-203, sections 712, 761(b), 124 Stat. 1754 (2010), and 15 U.S.C. 78dd(c).

* * * * *

2. § 240.3a71-3 is amended by:

a. Adding paragraphs (a)(6) through (a)(9);
b. Adding paragraph (b)(1)(iii)(C); and
c. Adding paragraph (c).

The additions read as follows:

§ 240.3a71-3 Cross-border security-based swap dealing activity.

(a) * * *

(6) U.S. security-based swap dealer means a security-based swap dealer, as defined in section 3(a)(71) of the Act (15 U.S.C. 78c(a)(71)), and the rules and regulations thereunder, that is a U.S. person.

(7) Foreign security-based swap dealer means a security-based swap dealer, as defined in section 3(a)(71) of the Act (15 U.S.C. 78c(a)(71)), and the rules and regulations thereunder, that is not a U.S. person.

(8) U.S. business means:

(i) With respect to a foreign security-based swap dealer:

(A) Any security-based swap transaction entered into, or offered to be entered into, by or on behalf of such foreign security-based swap dealer, with a U.S. person (other than a transaction conducted through a foreign branch of that person); or

(B) Any security-based swap transaction arranged, negotiated, or executed by personnel of the foreign security-based swap dealer located in a U.S. branch or office, or by personnel of an agent of the foreign security-based swap dealer located in a U.S. branch or office; and

(ii) With respect to a U.S. security-based swap dealer, any transaction by or on behalf of such U.S. security-based swap dealer, wherever entered into or offered to be entered into, other than a transaction conducted through a foreign branch with a non-U.S. person or with a U.S.-person counterparty that constitutes a transaction conducted through a foreign branch of the counterparty.

(9) Foreign business means security-based swap transactions that are entered into, or offered to be entered into, by or on behalf of, a foreign security-based swap dealer or a U.S. security-based swap dealer, other than the U.S. business of such person.

(b) * * *

(1) * * *

(iii) * * *

(C) Security-based swap transactions connected with such person's security-based swap dealing activity that are arranged, negotiated, or executed by personnel of such non-U.S. person located in a U.S. branch or office, or by personnel of an agent of such non-U.S. person located in a U.S. branch or office; and

* * * * *

(c) Application of customer protection requirements. A registered foreign security-based swap dealer and a registered U.S. security-based swap dealer, with respect to their foreign business, shall not be subject to the requirements relating to business conduct standards described in section 15F(h) of the Act (15 U.S.C. 78o-10(h)), and the rules and regulations thereunder, other than the rules and regulations prescribed by the Commission pursuant to section 15F(h)(1)(B) of the Act (15 U.S.C. 78o-10(h)(1)(B)).

3. § 240.3a71-5 is amended by adding paragraph (c) to read as follows:

§ 240.3a71-5 Exception for cleared transactions executed on a swap execution facility.

* * * * *

(c) The exceptions in paragraphs (a) and (b) of this section shall not apply to any security-based swap transactions of a non-U.S. person connected with its security-based swap dealing activity that are arranged, negotiated, or executed by personnel of such non-U.S. person located in a U.S. branch or office, or by personnel of an agent of such non-U.S. person located in a U.S. branch or office.

* * * * *

PART 242 — REGULATIONS M, SHO, ATS, AC, NMS, AND SCI AND CUSTOMER MARGIN REQUIREMENTS FOR SECURITY FUTURES

4. The authority citation for part 242 continues to read as follows:

Authority: 15 U.S.C. 77g, 77q(a), 77s(a), 78b, 78c, 78g(c)(2), 78i(a), 78j, 78k-l(c), 78*l*, 78m, 78n, 78o(b), 78o(c), 78o(g), 78q(a), 78q(b), 78q(h), 78w(a), 78dd-1, 78mm, 80a-23, 80a-29, and 80a-37.

5. § 242.900 is further amended, as proposed at 80 FR 14801 (March 19, 2015), by:

a. In paragraph (u)(3), removing the period and adding in its place "; or"; and

b. Adding paragraph (u)(4) to read as follows:

§ 242.900 Definitions

* * * * *

(u) * * *

(4) A registered broker-dealer (including a registered security-based swap execution facility) that is required to report a security-based swap to that registered security-based swap data repository by § 242.901(a).

* * * * *

6. § 242.901 is amended by:

a. Adding paragraphs (a)(2)(ii)(E)(2) through (4); and

b. Revising paragraph (d)(9).

The additions and revision read as follows:

§ 242.901 Reporting obligations.

(a) * * *

(2) * * *

(ii) * * *

(E) * * *

(2) If one side includes a non-U.S. person that falls within § 242.908(b)(5) or a U.S. person and the other side includes a non-U.S. person that falls within rule § 242.908(b)(5), the sides shall select the reporting side.

(3) If one side includes only non-U.S. persons that do not fall within § 242.908(b)(5) and the other side includes a non-U.S. person that falls within rule § 242.908(b)(5) or a U.S. person, the side including a non-U.S. person that falls within rule § 242.908(b)(5) or a U.S. person shall be the reporting side.

(4) If neither side includes a U.S. person and neither side includes a non-U.S. person that falls within § 242.908(b)(5) but the security-based swap is effected by or through a registered broker-dealer (including a registered security-based swap execution facility), the registered broker-dealer (including a registered security-based swap execution facility) shall report the information required by §§ 242.901(c) and 242.901(d).

* * * * *

(d) * * *

(9) The platform ID, if applicable, or if a registered broker-dealer (including a registered security-based swap execution facility) is required to report the security-based swap by § 242.901(a)(2)(ii)(E)(4), the broker ID of that registered broker-dealer (including a registered security-based swap execution facility);

* * * * *

7. § 242.906 is amended by revising paragraphs (b) and (c) to read as follows:

§ 242.906 Other duties of participants.

(a) * * *

(b) Duty to provide ultimate parent and affiliate information. Each participant of a registered security-based swap data repository that is not a platform, a registered clearing agency, or a registered broker-dealer (including a registered security-based swap execution facility) that becomes a participant solely as a result of making a report to satisfy an obligation under § 242.901(a)(2)(ii)(E)(4) shall provide to the registered security-based swap data repository information sufficient to identify its ultimate parent(s) and any affiliate(s) of the participant that also are participants of the registered security-based swap data repository, using ultimate parent IDs and counterparty IDs. Any such participant shall promptly notify the registered security-based swap data repository of any changes to that information.

(c) Policies and procedures to support reporting compliance. Each participant of a registered security-based swap data repository that is a security-based swap dealer, major security-based swap participant, registered clearing agency, registered broker-dealer (including a registered security-based swap execution facility) that becomes a participant solely as a result of making a report to satisfy an obligation under § 242.901(a)(2)(ii)(E)(4), or platform shall establish, maintain, and enforce written policies and procedures that are reasonably designed to ensure that it complies with any obligations to report information to a registered security-based swap data repository in a manner consistent with §§ 242.900 through 242.909. Each such participant shall review and update its policies and procedures at least annually.

* * * * *

8. § 242.907 is amended by revising paragraph (a)(6) to read as follows:

§ 242.907 Policies and procedures of registered security-based swap data repositories.

(a) * * *

(6) For periodically obtaining from each participant other than a platform, a registered clearing agency, or a registered broker-dealer (including a registered security-based swap execution facility) that becomes a participant solely as a result of making a report to satisfy an obligation under § 242.901(a)(2)(ii)(E)(4) information that identifies the participant's ultimate parent(s) and any participant(s) with which the participant is affiliated, using ultimate parent IDs and counterparty IDs.

* * * * *

9. § 242.908 is amended by adding paragraphs (a)(1)(iii) through (v); and is further amended as proposed at 80 FR 14801 (March 19, 2015), by adding paragraph (b)(5) to read as follows:

§ 242.908 Cross-border matters.

(a) * * *

(1) * * *

(iii) The security-based swap is executed on a platform having its principal place of business in the United States;

(iv) The security-based swap is effected by or through a registered broker-dealer (including a registered security-based swap execution facility); or

(v) The transaction is connected with a non-U.S. person's security-based swap dealing activity and is arranged, negotiated, or executed by personnel of such non-U.S. person located in a U.S. branch or office, or by personnel of an agent of such non-U.S. person located in a U.S. branch or office.

* * * * *

(b) * * *

(5) A non-U.S. person that, in connection with such person's security-based swap dealing activity, arranged, negotiated, or executed the security-based swap using its personnel located in a U.S. branch or office, or using personnel of an agent located in a U.S. branch or office.

By the Commission.

Dated: April 29, 2015

Brent J. Fields
Secretary

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