

**The Securities and Exchange Commission’s  
Implementation of Title VII of the Dodd-Frank Act:  
Reviewing the Status of Security-based Swap Market Regulation**

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**I. Introduction**

Gary Gensler served as Chair of the Commodity Futures Trading Commission (“CFTC”) from May 26, 2009 to January 3, 2014.<sup>2</sup> He presided over the CFTC during the period that followed the 2008 financial crisis and led the CFTC through the development and implementation of Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”). During that time, the CFTC established new rules related to the trading, clearing, and reporting of swaps and fundamentally changed the over-the-counter swaps market regulatory framework. Chair Gensler calculated that, during his tenure, the CFTC completed “over 170 Dodd-Frank actions - nearly one a week since it was signed into law.”<sup>3</sup>

On April 17, 2021, Mr. Gensler was sworn in as Chair of the Securities and Exchange Commission (“SEC”). Over the last 20 months, the SEC has moved rapidly to propose and consider a number of regulatory actions. In fact, industry groups<sup>4</sup> and legislators<sup>5</sup> have expressed concerns with Chair Gensler’s SEC’s pace of action.

More recently, before this American Bar Association Derivatives and Futures Law Committee, Chair Gensler provided remarks focused primarily on the regulation of the security-based swaps market and security-based swap execution facilities (“SBSEFs”).<sup>6</sup> Chair Gensler

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<sup>2</sup> About the CFTC, Former Commissioners, Chairman Gary Gensler, CFTC.

<sup>3</sup> Remarks of Chairman Gary Gensler at Farewell Event, Public Statements & Remarks, CFTC (Dec. 19, 2013).

<sup>4</sup> Letter from Investment Company Institute, et al, to SEC Chair Gary Gensler (Apr. 5, 2022).

<sup>5</sup> Letter from U.S. Senator Thom Tillis, et al, to SEC Chair Gary Gensler (Oct. 27, 2022).

<sup>6</sup> “Security-based swap execution facility” means “a trading system or platform in which multiple participants have the ability to execute or trade security-based swaps by accepting bids and offers made by multiple participants in the facility or system, through any means of interstate commerce, including any trading facility, that (A) facilitates the execution of security-based swaps between persons; and (B) is not a national securities exchange.” 15 U.S.C. § 78c(77).

discussed the new requirements under which security-based swap dealers (“SBSDs”)<sup>7</sup> and major security-based swap participants (“MSBSPs”)<sup>8</sup> were required to register with the SEC before the end of 2021, among other topics. Chair Gensler also discussed that the SEC has made a substituted compliance determination order and expects to receive and review substituted compliance applications for additional jurisdictions soon.<sup>9</sup>

During his SEC Chairmanship confirmation hearings, Chair Gensler committed to “complete all rulemakings directed by Congress,” including the outstanding Dodd-Frank Title VII rulemakings.<sup>10</sup> Since his confirmation, the SEC has moved forward with several security-based swap initiatives, including proposals related to fraud and manipulation, electronic recordkeeping, and SBSEF registration and trading, among other items. Staff in the Division of Trading and Markets have also provided interpretive guidance and no-action relief to facilitate the implementation of the SEC’s security-based swap rules.

This paper analyzes the SEC’s progress with respect to implementation of Title VII of Dodd-Frank for security-based swaps. The paper covers rules adopted and implemented by the SEC, proposals pending adoption, staff action by the Division of Trading and Markets, and highlights relevant cases brought by the SEC’s Division of Enforcement.

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<sup>7</sup> An SBSBD means any person who: (1) holds itself out as a dealer in security-based swaps; (2) makes a market in security-based swaps; (3) regularly enters into security-based swaps with counterparties as an ordinary course of business for its own account; or (4) engages in any activity causing it to be commonly known in the trade as a dealer or market maker in security-based swaps. 17 C.F.R. § 240.3a71-1(a).

<sup>8</sup> An MSBSP means any person:

(1) that is not a security-based swap dealer; and (2)(i) that maintains a substantial position in security-based swaps for any of the major security-based swap categories, excluding both positions held for hedging or mitigating commercial risk, and positions maintained by any employee benefit plan (or any contract held by such a plan) as defined in paragraphs (3) and (32) of section 3 of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1002) for the primary purpose of hedging or mitigating any risk directly associated with the operation of the plan; (ii) Whose outstanding security-based swaps create substantial counterparty exposure that could have serious adverse effects on the financial stability of the United States banking system or financial markets; or (iii) That is a financial entity that: (A) Is highly leveraged relative to the amount of capital such entity holds and that is not subject to capital requirements established by an appropriate Federal banking agency (as defined in 15 U.S.C. 78c(a)(72)); and (B) Maintains a substantial position in outstanding security-based swaps in any major security-based swap category. 17 C.F.R. § 240.3a67-1(a).

<sup>9</sup> “A ‘New’ New Era.” Prepared Remarks Before the International Swaps and Derivatives Association Annual Meeting, Chair Gary Gensler (May 11, 2022).

<sup>10</sup> Committee on Banking, Housing, and Urban Affairs Nominations of The Honorable Gary Gensler and The Honorable Rohit Chopra (Mar. 2, 2021).

## II. Adopted Rules

### A. Foundational Rules Jointly Adopted by the CFTC

On April 18, 2012, the SEC, jointly with the CFTC, adopted rules defining the terms “security-based swap dealer”<sup>11</sup> and “major security-based swap participant”<sup>12</sup> as part of the Securities Exchange Act of 1934 (“Exchange Act”).<sup>13</sup>

On July 9, 2012, the SEC and CFTC further interpreted the terms “swap” and “security-based swap” and whether a particular instrument is a “swap” regulated by the SEC.<sup>14</sup> The SEC and CFTC also addressed “mixed swaps” which are regulated by both agencies, and “security-based swap agreements,” which are regulated by the CFTC but over which the SEC has antifraud and other authority.<sup>15</sup>

### B. Security-based Swap Dealer Rules

#### i. Security-based Swap Dealer Registration

On August 5, 2015, the SEC adopted rules that lay out the process for entities to register as SBSDs and MSBSPs (collectively, “SBS Entities”).<sup>16</sup> The rules describe the process through which an SBS Entity can apply for registration with the SEC, and identify the various types of registration forms used for filings.<sup>17</sup> The rules also require an SBS Entity to promptly file an amendment when information in the registration form becomes inaccurate.<sup>18</sup> The rules also provide the process by which an SBS Entity may withdraw registration and by which the SEC may cancel or revoke the registration of an SBS Entity.<sup>19</sup> The rules also require an SBS Entity to provide two separate certifications by senior officers of the organization, and the certifications

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<sup>11</sup> See supra note 7.

<sup>12</sup> See supra note 8.

<sup>13</sup> Further Definition of “Swap Dealer,” “Security-Based Swap Dealer,” “Major Swap Participant,” “Major Security-Based Swap Participant” and “Eligible Contract Participant,” 77 FR 30,596 (May 23, 2012).

<sup>14</sup> Further Definition of “Swap,” “Security-Based Swap,” and “Security-Based Swap Agreement”; Mixed Swaps; Security-Based Swap Agreement Recordkeeping, 87 Fed Reg. 48, 208 (Aug. 13, 2012).

<sup>15</sup> *Id.*

<sup>16</sup> Registration Process for Security-Based Swap Dealers and Major Security-Based Swap Participants, 80 Fed. Reg. 48,963 (Aug. 14, 2015).

<sup>17</sup> *Id.*

<sup>18</sup> *Id.*

<sup>19</sup> *Id.*

would be required to be supported by appropriate due diligence.<sup>20</sup> The rules became effective October 13, 2015.<sup>21</sup> The compliance date for security-based swap dealer registration was November 1, 2021.<sup>22</sup>

ii. Security-based Swap Dealer De Minimis Exemption

On April 18, 2012, the SEC adopted Rule 3a71-2, which implements the de minimis exception. For instance, Rule 3a71-2 exempts those entities or individuals who engage in dealing activity in security-based swaps up to a certain notional dollar amount over a prior one-year period. With respect to credit default swaps (“CDS”) that are security-based swaps, the de minimis exception in general is available to persons who enter into up to \$3 billion in notional CDS dealing transactions over the prior 12 months. With respect to other types of security-based swaps, the threshold is \$150 million, reflecting the proportionately smaller size of this part of the market. In addition, Rule 3a71-2 sets a different de minimis exception for security-based swaps with “special entities” (as defined in Exchange Act Section 15F(h)(2)(C) to include certain governmental and other entities). With respect to those special entities, the threshold is \$25 million in notional amount over the prior 12 months. Additionally, neither limits the number of security-based swaps that a person can enter, nor limits the number of a person’s security-based swap counterparties in a dealing capacity.<sup>23</sup> The rule also permits an entity that would otherwise satisfy the de minimis exception to register as an SBSB.<sup>24</sup> The rules became effective on July 23, 2012.<sup>25</sup> Since August 6, 2021, the SEC noted that market participants should assess whether they meet the definition of “security-based swap dealer,” including whether they are able to continue to satisfy the de minimis exception after counting security-based swap dealing activity engaged in on or after that date.<sup>26</sup>

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<sup>20</sup> The first certification requires a senior officer of the applicant to certify that, after due inquiry, he or she has reasonably determined that the applicant has developed and implemented written policies and procedures reasonably designed to prevent violations of the federal securities laws and the rules thereunder, and that he or she has documented the process by which he or she reached such determination. The second certification requires the Chief Compliance Officer (CCO), or his or her designee, to certify that the CCO neither knows, nor in the exercise of reasonable care should have known, that any person associated with the SBS Entity who effects or is involved in effecting security-based swaps on its behalf is subject to a statutory disqualification, unless otherwise specifically provided by rule, regulation or order of the Commission. This rule also would require that, to support the certification, the CCO, or his or her designee, must review and sign the questionnaire or application for employment executed by associated persons who are natural persons and who effect or are involved in effecting securities-based swaps on the SBS Entity’s behalf. *Id.*

<sup>21</sup> *Id.*

<sup>22</sup> Key Dates for Registration of Security-Based Swap Dealers and Major Security-Based Swap Participants, SEC.

<sup>23</sup> Further Definition of “Swap Dealer,” “Security-Based Swap Dealer,” “Major Swap Participant,” “Major Security-Based Swap Participant” and “Eligible Contract Participant,” 77 FR 30,596 (May 23, 2012).

<sup>24</sup> Note, for an entity that does not meet the definition of “security-based swap dealer,” voluntary registration with the SEC as a security-based swap dealer causes the person to be deemed to be a security-based swap dealer. 17 C.F.R. § 240.3a71-3(e)

<sup>25</sup> *Id.*

<sup>26</sup> Key Dates for Registration of Security-Based Swap Dealers and Major Security-Based Swap Participants, SEC.

### iii. Capital, Margin, and Segregation Requirements

On June 21, 2019, the SEC adopted a package of rules and rule amendments that set forth the capital, margin and segregation requirements for SBSDs and MSBSPs. These rules establish the minimum capital requirements for SBSDs and MSBSPs for which there is not a prudential regulator (nonbank SBSDs and MSBSPs).<sup>27</sup> The rules also increase the minimum net capital requirements for broker-dealers that use internal models to compute net capital (ANC broker-dealers). Nonbank SBSDs that use models to compute net capital and ANC broker-dealers are subject to minimum tentative net capital requirements (tentative net capital equals net capital before deducting standardized haircuts or, in the case of firms that use models, market and credit risk charges).<sup>28</sup> Nonbank SBSDs and ANC broker-dealers are subject to minimum net capital requirements that are the greater of a fixed-dollar amount and an amount equal to 2% of the firm's exposures to its security-based swap customers (2% margin factor) plus, in the case of broker-dealer SBSDs and ANC broker-dealers, the existing ratio-based minimum net capital requirements in Rule 15c3-1 (either the 15-to-1 aggregate indebtedness ratio or the 2% of customer debit items ratio).<sup>29</sup> Nonbank SBSDs that are not broker-dealers (other than an OTC derivatives dealer) will be subject to only a 2% margin factor ratio.<sup>30</sup>

The rules also establish the margin requirements for nonbank SBSDs and MSBSPs with respect to non-cleared security-based swaps. Nonbank SBSDs will be required to calculate with respect to each account of a counterparty as of the close of business each day: (1) the amount of current exposure in the account (i.e., variation margin) and (2) the initial margin amount for the account. Nonbank MSBSPs will be required to collect collateral from or deliver collateral to a counterparty to cover a variation margin requirement, unless an exception applies. The rule does not require nonbank MSBSPs to collect or deliver initial margin.<sup>31</sup>

The rules also describe the segregation requirements for SBSDs and stand-alone broker-dealers for cleared and non-cleared security-based swaps. Namely, the rules require SBSDs and broker-dealers to segregate money, securities, and property of a security-based swap customer relating to a cleared or non-cleared security-based swap, but to do so in a manner that permits the assets to be commingled with money, securities, or property of other customers (omnibus segregation).<sup>32</sup>

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<sup>27</sup> Capital, Margin, and Segregation Requirements for Security-Based Swap Dealers and Major Security-Based Swap Participants and Capital and Segregation Requirements for Broker-Dealers, 84 Fed. Reg. 43,872 (August 22, 2019).

<sup>28</sup> *Id.*

<sup>29</sup> *Id.*

<sup>30</sup> *Id.*

<sup>31</sup> *Id.*

<sup>32</sup> *Id.*

These rules became effective on October 21, 2019.<sup>33</sup> The compliance date for these rules was October 6, 2021.<sup>34</sup>

#### iv. Recordkeeping and Reporting Requirements

On September 19, 2019, the SEC adopted new rules and amendments establishing recordkeeping and reporting requirements for SBSBs, MSBSPs and broker-dealers. The rules, among other things: (1) establish the record making requirements for SBSBs and MSBSPs and amend the existing record making requirements for broker-dealers to account for their security-based swap activities; (2) establish the record preservation requirements for SBSBs and MSBSPs and amend the existing record preservation requirements for broker-dealers to address records relating to their security-based swap activities; (3) establish the periodic reporting and annual audit requirements for SBSBs and MSBSPs and amend the existing reporting requirements for broker-dealers to account for their security-based swap activities; (4) establish early warning notification requirements for SBSBs and MSBSPs; (5) establish security count requirements for SBSBs that are not registered as broker-dealers and do not have a prudential regulator (stand-alone SBSBs); (6) amend the SEC's existing cross-border rule to provide a means to request substituted compliance with respect to the recordkeeping and reporting requirements for SBSBs and MSBSPs; and (7) amend a rule that permits certain SBSBs that are registered as swap dealers and predominantly engage in a swaps business to comply with CFTC requirements in lieu of SEC requirements.<sup>35</sup> The rules became effective on February 14, 2020.<sup>36</sup> The compliance date for these rules was October 6, 2021.<sup>37</sup>

In addition, on October 12, 2022, the SEC voted to adopt amendments to the electronic recordkeeping requirements for broker-dealers and security-based swap dealers contained in Rules 17a-4 and 18a-6, respectively. The amendments, which are intended to make SEC recordkeeping requirements more technology neutral than they currently are, modify the rules by: (1) adding an audit-trail alternative to the existing requirement that broker-dealers preserve electronic records exclusively in a non-rewriteable, non-erasable format; (2) requiring that, to meet the audit-trail alternative, a broker-dealer's electronic recordkeeping system must preserve electronic records in a manner that permits the recreation of an original record if it is altered, over-written, or erased; (3) requiring that nonbank SBSBs and MSBSPs preserve electronic records in a manner that meets the audit-trail requirement, or exclusively in a non-rewriteable, non-erasable format; (4) requiring that broker-dealers, SBSBs, and MSBSPs produce electronic records in a reasonably usable electronic format to allow securities regulators to search and sort information on the records; (5) adding to the existing requirement in the broker-dealer recordkeeping rule that the firm hire a third party with the ability to access the firm's electronic records that undertakes to provide the records

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<sup>33</sup> *Id.*

<sup>34</sup> Key Dates for Registration of Security-Based Swap Dealers and Major Security-Based Swap Participants, SEC.

<sup>35</sup> Recordkeeping and Reporting Requirements for Security-Based Swap Dealers, Major Security-Based Swap Participants, and Broker-Dealers, 84 Fed. Reg. 68,550 (Dec. 16, 2019).

<sup>36</sup> *Id.*

<sup>37</sup> Key Dates for Registration of Security-Based Swap Dealers and Major Security-Based Swap Participants, SEC.

to securities regulators if the firm fails or is unable to do so with an alternative that a designated executive officer of the firm can undertake this responsibility; (6) adding a parallel third party or designated executive officer requirement to the SBS and MSBSP electronic recordkeeping requirements rule; (7) eliminating a requirement that a broker-dealer notify its designated examining authority before employing an electronic recordkeeping system; and (8) adding an alternative approach to the undertaking that must be obtained from a third party that holds electronic records for a broker-dealer, SBS, or MSBSP to accommodate the practice of using a recordkeeping service, including a cloud service provider, for this purpose.<sup>38</sup> The rules become effective on January 3, 2023.<sup>39</sup>

v. Business Conduct Standards

On April 15, 2016, the SEC adopted rules implementing a comprehensive set of business conduct standards and chief compliance officer requirements for SBSs and MSBSPs. SBS entities must comply with a bevy of provisions designed to enhance transparency, facilitate informed customer decision-making, and heighten standards of professional conduct. For example, SBS entities are required to deal fairly with potential counterparties by communicating in a fair and balanced manner, disclosing material information about the security-based swap, including material risks, characteristics, incentives and conflicts of interest, and adhering to other professional standards of conduct. There are also additional requirements that apply for dealings with special entities, which include municipalities, pension plans, endowments, and similar entities. The rules also establish supervision and chief compliance officer requirements. In addition, the rules address the cross-border application of these requirements and the potential availability of substituted compliance.<sup>40</sup> The rules became effective on July 12, 2016. The compliance date for these rules was October 6, 2021.<sup>41</sup>

vi. Trade Acknowledgement and Verification

On June 8, 2016, the SEC adopted rules designed to establish timely and accurate trade acknowledgement and verification requirements for SBSs and MSBSPs that enter into security-based swap transactions. The rules require SBS entities to provide a trade acknowledgment that contains all of the terms of the transaction. Specifically, the rules require SBSs and MSBSPs to: (1) provide a trade acknowledgment electronically to its transaction counterparty promptly, and no later than the end of the first business day following the day of execution; (2) promptly verify or dispute with its counterparty the terms of a trade acknowledgment it receives; (3) have written policies and procedures in place that are reasonably designed to obtain verification of the terms

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<sup>38</sup> SEC Adopts Rule Amendments to Modernize How Broker-Dealers Preserve Electronic Records and Enhance the Electronic Recordkeeping Requirements for Security-Based Swap Entities, 87 Fed. Reg. 66,412 (Nov. 3, 2022).

<sup>39</sup> The compliance date for the amendments to Rule 17a-4 is May 3, 2023, and the compliance date for the amendments to Rule 18a-6 is November 3, 2023. *Id.*

<sup>40</sup> Business Conduct Standards for Security-Based Swap Dealers and Major Security-Based Swap Participants, 81 Fed. Reg. 29,959 (May 13, 2016).

<sup>41</sup> Key Dates for Registration of Security-Based Swap Dealers and Major Security-Based Swap Participants, SEC.

outlined in any trade acknowledgment that it provides.<sup>42</sup> This rule became effective on August 16, 2016, but was not fully implemented until the security-based swap entity registration rules went into effect. The compliance date for these rules was October 6, 2021.<sup>43</sup>

vii. Risk Mitigation Techniques

On December 18, 2019, the SEC adopted rules requiring the application of risk mitigation techniques to portfolios of uncleared security-based swaps. These rules establish requirements for SBSDs and MSBSPs to: (1) periodically reconcile outstanding security-based swaps with counterparties; (2) engage in certain forms of portfolio compression exercises, as appropriate; and (3) execute written trading relationship documentation with each of their counterparties prior to, or contemporaneously with, executing a security-based swap transaction.<sup>44</sup> The rules became effective on April 6, 2020, but were not fully implemented until the security-based swap entity registration rules went into effect.<sup>45</sup> The compliance date for these rules was October 6, 2021.<sup>46</sup>

C. *Security-based Swap Clearing*

On March 30, 2012, the SEC adopted rules exempting certain security-based swap transactions cleared by security-based swap clearing agencies from: (1) all of the requirements of the Securities Act of 1933 (Securities Act) other than the antifraud provisions of Section 17(a), but including the registration requirements of Section 5; and (2) the registration requirements of Sections 12(a) and 12(g) of the Securities Exchange Act of 1934. These rules cover all cleared SBS, including most cleared CDS, that are: (1) cleared by clearing agencies that are either registered with the SEC or exempt from registering; and (2) entered into by eligible contract participants (“ECP”), as defined under the Commodity Exchange Act. The final rules become effective on April 16, 2012.<sup>47</sup>

On June 28, 2012, the SEC adopted rules that establish procedures for its review of certain clearing agency actions. A clearing agency must file information with the SEC regarding any security-based swap—or any group, category, type, or class of security-based swaps—that a clearing agency plans to accept for clearing. These submissions must be filed electronically with the SEC using the existing Electronic Form 19b-4 Filing System and Form 19b-4. The SEC also adopted rules that define and describe when a designated “systemically important” clearing agency is required to provide advance notice to the SEC before it makes certain changes to its rules, procedures, or operations. Such “advance notices” must be filed when: (1) the proposed change

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<sup>42</sup> Trade Acknowledgment and Verification of Security-Based Swap Transactions, 81 Fed. Reg. 39,807 (Jun. 17, 2016).

<sup>43</sup> Key Dates for Registration of Security-Based Swap Dealers and Major Security-Based Swap Participants, SEC.

<sup>44</sup> Risk Mitigation Techniques for Uncleared Security-Based Swaps, 85 Fed. Reg. 6,539 (Feb. 4, 2020).

<sup>45</sup> *Id.*

<sup>46</sup> Key Dates for Registration of Security-Based Swap Dealers and Major Security-Based Swap Participants, SEC.

<sup>47</sup> Exemptions for Security-Based Swaps Issued by Certain Clearing Agencies, 77 Fed. Reg. 20,536 (Apr. 5, 2012).

would affect the risk management functions performed by the clearing agency that are related to systemic risk; or (2) the proposed change could affect the clearing agency's ability to continue to perform its core clearance and settlement functions.<sup>48</sup> The SEC also adopted rules that: (1) establish the procedure by which the SEC may stay the mandatory clearing requirement at the request of a counterparty to the security-based swap or on the SEC's own initiative; (2) seek to prevent evasion of the clearing requirement by clarifying that clearing needs to occur through a central counterparty; and (3) make form and rule changes to reflect new deadlines under the Dodd-Frank Act for proposed rule changes by self-regulatory organizations.<sup>49</sup> The rules became effective August 13, 2012.<sup>50</sup>

On October 22, 2012, the SEC adopted a rule that establishes standards for how registered clearing agencies should manage their risks and run their operations. Among other requirements, the rule requires a registered clearing agency that performs central counterparty services to establish, implement, maintain and enforce written policies and procedures reasonably designed to maintain sufficient financial resources to withstand, at a minimum, a default by the participant family to which it has the largest exposure in extreme but plausible market conditions (and a default by the two participant families to which it has the largest exposures for security-based swap clearing agencies). Additionally, a registered clearing agency that performs central counterparty services is required to establish, implement, maintain, and enforce written policies and procedures reasonably designed to provide the opportunity to obtain membership in the clearing agency for persons who are not dealers or security-based swap dealers on fair and reasonable terms.<sup>51</sup> The rule became effective on January 2, 2013.<sup>52</sup>

On December 16, 2020, the SEC adopted a rule to limit the potential for overlapping or duplicative regulation within its security-based swap regulatory regime. Specifically, the rule exempts certain activities of security-based swap execution facilities and security-based swap dealers from triggering the requirement also to register as a clearing agency, in line with similar exemptions for broker-dealers and national securities exchanges.<sup>53</sup> This rule became effective on April 2, 2021.<sup>54</sup>

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<sup>48</sup> Changes that could require advance notice may include, but are not limited to, changes that materially affect participant and product eligibility, risk management, daily or intraday settlement procedures, default procedures, system safeguards, governance, or financial resources of the designated clearing agency.

<sup>49</sup> Process for Submissions for Review of Security-Based Swaps for Mandatory Clearing and Notice Filing Requirements for Clearing Agencies; Technical Amendments to Rule 19b-4 and Form 19b-4 Applicable to All Self-Regulatory Organizations, 77 Fed. Reg. 41,602 (Jul. 13, 2012).

<sup>50</sup> *Id.*

<sup>51</sup> Clearing Agency Standards, 77 Fed. Reg. 66,220 (Nov. 2, 2012).

<sup>52</sup> *Id.*

<sup>53</sup> Exemption from the Definition of "Clearing Agency" for Certain Activities of Security-Based Swap Dealers and Security-Based Swap Execution Facilities, 86 Fed. Reg. 7,637 (Feb. 1, 2021).

<sup>54</sup> *Id.*

D. *Post-Trade Reporting and Public Dissemination of Security-based Swap Transactions*

On July 13, 2016, the SEC adopted amendments and guidance related to rules regarding the regulatory reporting and public dissemination of security-based swap transactions, known as Regulation SBSR. Regulation SBSR: (1) requires a national securities exchange or security-based swap execution facility to report a security-based swap executed on the platform that will be submitted to clearing; (2) requires a registered clearing agency to report any security-based swap to which it is a direct counterparty, as well as whether or not the clearing agency accepts a transaction for clearing; (3) prohibits a registered swap data repository (“SDR”) from imposing fees or usage restrictions on the security-based swap transaction data that it is required by Regulation SBSR to publicly disseminate; (4) requires any 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 its agent located in a U.S. branch or office—to be reported and publicly disseminated; (5) provides guidance regarding the application of Regulation SBSR to security-based swaps resulting from prime brokerage arrangements and from the allocation of cleared security-based swaps; and (6) establishes a compliance schedule for the portions of Regulation SBSR for which the Commission has not previously specified compliance dates.<sup>55</sup> These rules became effective on October 11, 2016, but were not fully implemented until the security-based swap entity registration rules went into effect.

**III. Proposed Rules Not Yet Adopted**

A. *Registration and Regulation of Security-Based Swap Execution Facilities*

On April 6, 2022, the SEC proposed new Regulation SE to create a regime for the registration and regulation of SBSEFs. An entity that meets the definition of an SBSEF must register as an SBSEF on Form SBSEF or register as a national securities exchange.<sup>56</sup> A registered SBSEF would be required to: (1) submit filings with the SEC for new rules, rule amendments, or products; (2) submit information to the Commission that the Commission requests, including demonstrations that the SBSEF is in compliance with one or more Core Principles, notification of a transfer of 50 percent or more of the equity interest in the SBSEF, and information about pending legal proceedings; (3) establish, comply with, and enforce its rules, including, among others, rules regarding market access, trading and trade processing, the operation of the SBSEF, the financial integrity of SBS on its facility, the exercise of emergency authority, and conflicts of interest; (4) monitor trading and market activity to prevent manipulation, price distortion, and delivery or settlement disruptions; (5) make public timely information on price, trading volume, and other trading data on SBS transactions, as required by Regulation SBSR, and publish on its website a Daily Market Data Report; (6) maintain records of all activities relating to the business of the facility, including a complete audit trail, in a form and manner acceptable to the Commission, for a period of five years; (7) have adequate financial, operational, and managerial resources to

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<sup>55</sup> Regulation SBSR—Reporting and Dissemination of Security-Based Swap Information, 81 Fed. Reg. 53,546 (Aug. 12, 2016).

<sup>56</sup> The proposal provides that Foreign SBS trading venues may seek an exemption from the definition of SBSEF pursuant to proposed Rule 8333(a).

discharge its responsibilities; (8) establish and maintain a program of automated systems and risk analysis to identify and minimize sources of operational risk, through the development of appropriate controls and procedures; (9) establish and maintain emergency procedures, backup facilities, and a disaster recovery plan; and (10) designate a CCO and establish regulatory and reporting obligations for the CCO.<sup>57</sup>

B. *Prohibition Against Fraud, Manipulation, or Deception in connection with Security-Based Swaps*

On December 15, 2021, the SEC proposed a set of rules designed to prevent fraud, manipulation and deception in connection with security-based swaps, to prevent undue influence over the CCO of SBS Entities, and to require any person with a large security-based swap position to publicly report certain information related to the position.<sup>58</sup> Proposed Rule 9j-1 would: (1) prohibit a bevy of misconduct and attempted misconduct in connection with security-based swaps, including misconduct in connection with the exercise of any right or performance of any obligation under a security-based swap; (2) prohibit manipulation or attempted manipulation of the price or valuation of any security-based swap, or any payment or delivery related thereto; (3) provide limited safe harbors for certain specified conduct; and (4) provide that a person cannot escape liability for trading based on possession of material non-public information about a security by purchasing or selling a security-based swap based on that security and cannot escape liability under the proposed rule by purchasing or selling the underlying security (as opposed to purchasing or selling a security-based swap that is based on that security).<sup>59</sup>

Proposed Rule 15Fh-4(c) would prohibit any officer, director, supervised person or employee of an SBS Entity, or any person acting under such person's direction, to take any action to coerce, manipulate, mislead, or fraudulently influence the SBS Entity's CCO in the performance of their duties under the federal securities laws.<sup>60</sup>

Proposed Rule 10B-1 would (1) require any person, or group of persons, with a security-based swap position that exceeds a specified reporting threshold to promptly file a Schedule 10B disclosing certain information related to its position; (2) provide that any Schedule 10B be filed promptly, but in no event later than the end of the first business day following the day of execution of the security-based swap transaction that results in the security-based swap position exceeding

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<sup>57</sup> In developing the proposal, the SEC sought to harmonize, as closely as practicable, the CFTC's rules that govern swap execution facilities and swap execution generally. SEC Proposes Rules for the Registration and Regulation of Security-Based Swap Execution Facilities, 87 Fed. Reg. 28,872 (May 11, 2022).

<sup>58</sup> Section 761(a)(2) of the Dodd-Frank Act amends the definition of "security" in Section 3(a)(10) of the Exchange Act to include security-based swaps and Section 768(a)(1) of the Dodd-Frank Act amends the definition of "security" in Section 2(a)(1) of the Securities Act to include security-based swaps. As such, security-based swaps are subject to the general antifraud and anti-manipulation provisions of the federal securities laws (e.g., Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, and Section 17(a) of the Securities Act of 1933). See Prohibition Against Fraud, Manipulation, and Deception in Connection With Security-Based Swaps, Proposed Rule, 75 Fed. Reg. 68,560 (Nov. 8, 2010).

<sup>59</sup> Prohibition Against Fraud, Manipulation, or Deception in Connection with Security-Based Swaps; Prohibition against Undue Influence over Chief Compliance Officers; Position Reporting of Large Security-Based Swap Positions 87 Fed. Reg. 6,652 (Feb. 4, 2022).

<sup>60</sup> *Id.*

threshold; and (3) require reporting persons to file amendments promptly in the event of any material change to a previously filed Schedule 10B.<sup>61</sup>

Schedule 10B would require persons to disclose certain information including: the identity of the reporting person and the security-based swap position, as well as the underlying loans or securities and any related loans and securities.<sup>62</sup>

#### **IV. Division of Trading & Markets Action Related to Security-based Swaps**

The Trading and Markets staff (“T&M staff”) has provided no-action relief from various requirements applicable to SBSBs. For example, the T&M staff has granted no-action relief under the SBSB risk management rule (Rule 15c3-4), the SBSB capital rule (Rule 18a-1), and the SBSB reporting rule (Rule 18a-7) if an SBSB incorporates certain reviews and reports identified for its first fiscal year ending after the date it registered as an SBSB into the reviews and reports for the second fiscal year.<sup>63</sup> The T&M staff also has granted no-action relief with respect to the capital requirements under section 15F of the Exchange Act and Rules 18a-1, 18a-1a, 18a-1b, 18a-1c, and 18a-1d, certain recordkeeping requirements of Rules 18a-5 and 18a-6, certain reporting requirements of Rule 18a-7, and certain notification requirements of Rule 18a-8 for an entity that operates as if it was eligible to apply substituted compliance with respect to these requirements pursuant to the terms and conditions of the order of the SEC granting substituted compliance in connection with certain requirements applicable to security-based swap dealers (“SBSBs”) in the Federal Republic of Germany.<sup>64</sup>

The staff granted no-action relief under section 15F(f) of the Exchange Act and Rule 18a-7(a)(2) thereunder to entities if they register with the Commission as SBSBs and file periodic unaudited financial and operational information with the Commission or its designee pursuant to Rule 18a-7(a)(2) in accordance with the Manner and Format Order and presents the financial information in the filing in accordance with Australian GAAP, Canadian GAAP, and Swedish GAAP, respectively.<sup>65</sup>

The T&M staff also granted no-action relief under Exchange Act section 15F(f) and Rule 18a-7 thereunder if a stand-alone SBSB makes public on its website the firm’s midyear unaudited financial statements within 55 calendar days of the date of the statements.<sup>66</sup> The T&M staff also granted no-action relief if a nonbank SBSB, for purposes of Exchange Act Rule 18a-3(c)(1)(ii)(B),

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<sup>61</sup> *Id.*

<sup>62</sup> *Id.*

<sup>63</sup> SIFMA (Feb. 23, 2022).

<sup>64</sup> Morgan Stanley Europe SE (Dec. 22, 2021).

<sup>65</sup> Macquarie Bank Limited (Nov. 19, 2021); Canadian Banks Association (Nov. 1, 2021); Skandinaviska Enskilda Banken AB (Nov. 1, 2021).

<sup>66</sup> SIFMA (Oct. 27, 2021).

does not collect initial margin from a Phase 6+ Counterparty<sup>67</sup> in connection with non-cleared security-based swaps entered into with such counterparty before September 1, 2022, provided the nonbank SBSB makes a record of such Phase 6+ Counterparties, and preserves the record for a period of not less than three years, the first two years in an easily accessible place.<sup>68</sup>

## V. SEC Security-based Swap Enforcement Cases

The SEC has brought several enforcement actions against firms for offering and selling unregistered security-based swaps and failing to transact its swaps on a registered national exchange.<sup>69</sup> These cases, to date, have focused on unregistered security-based swap activity and has not yet touched on SBSB regulatory compliance. At the same time, the SEC remains focused on certain security-based swap activity, such as the use of total return swaps in the Archegos Capital Management, LP matter.<sup>70</sup>

For instance, the SEC found that Tradenet Capital Markets Ltd. offered and sold security-based swaps to over 5,000 retail investors without registration and failed to transact its swaps on a registered national exchange.<sup>71</sup> There, Tradenet sold investors packages of materials that claimed to be for the purpose of educating investors about day trading, but also paid investors a portion of net profits from simulated trades conducted in a funded trading account provided as part of the packages.<sup>72</sup> Tradenet charged from \$500 to \$9,000 for the educational packages that included the simulated trading accounts.<sup>73</sup> Investors, whose portfolios increased in value, received payouts equal to a percentage of the simulated net profits, but if the value of the portfolio decreased by a certain amount, the funded trading account was closed.<sup>74</sup>

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<sup>67</sup> A Phase 6+ Counterparty means a counterparty to a non-cleared security-based swap that, combined with all of its affiliates has a daily aggregate notional amount of non-cleared swaps, non-cleared security-based swaps, foreign exchange swaps, and foreign exchange forwards in March, April, and May 2021 of \$50 billion or less. ISDA and SIFMA (Aug. 5, 2021).

<sup>68</sup> *Id.*

<sup>69</sup> In the Matter of Tradenet Capital Markets LTD, File No. 3-20137 (Oct. 23, 2020); In the Matter of Plutus Financial Inc. d/b/a Abra and Plutus Technologies Philippines Corp, File No. 3-19873 (Jul. 13, 2020); In the Matter of XBT Corp Sarl d/b/a/ First Global Credit, File No. 3-19592 (Oct. 31, 2019); In the Matter of Equidate, Inc. and Equidate Holdings LLC, File No. 3-17708 (Dec. 6, 2016); In the Matter of Forcerank LLC, File No. 3-17625 (Oct. 13, 2016); In the Matter of Sand Hill Exchange, Gerrit Hall, and Elaine Ou, File No. 3-16598 (June 17, 2015).

<sup>70</sup> The CFTC also brought a parallel case in front of the Southern District of New York against Archegos Capital and Archegos' Chief Financial Officer. The U.S. Attorney for the Southern District of New York brought criminal charges against the founder of Archegos, as well as Archegos' Chief Financial Officer. *SEC v. Sung Kook (Bill) Hwang Patrick Halligan, William Tomita, Scott Becker, and Archegos Capital Management, LP*, Case 1:22-cv-03402 (S.D.N.Y. 2022); *CFTC v. Archegos Capital Management, LP and Patrick Halligan*, Case 1:22-CV-03401 (S.D.N.Y. 2022); *United States v. Sung Kook (Bill) Hwang and Patrick Halligan*, Case 22 Crim 240 (S.D.N.Y. 2022).

<sup>71</sup> In the Matter of Tradenet Capital Markets LTD, File No. 3-20137 (Oct. 23, 2020).

<sup>72</sup> *Id.*

<sup>73</sup> *Id.*

<sup>74</sup> *Id.*

In another action, the SEC found that XBT Corp. Sarl (“XBT”) offered and sold unregistered security-based swaps to U.S. retail investors using bitcoins and failed to transact its swaps on a registered national exchange.<sup>75</sup> XBT used a variety of marketing methods to target and solicit U.S. individuals to deposit and use bitcoins to buy and sell a variety of investment products.<sup>76</sup> Although XBT used different terminology to describe the investments it offered, including “bitcoin Asset Linked Notes,” investors were able to participate in the price movements of securities, including those listed on U.S. securities exchanges, without owning them.<sup>77</sup>

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<sup>75</sup> In the Matter of XBT Corp Sarl d/b/a/ First Global Credit, File No. 3-19592 (Oct. 31, 2019).

<sup>76</sup> *Id.*

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