

# A step closer

The SEC still has some work to do to finalise its framework for SBS dealer registration but firms are already expected to set compliance plans in motion

**M**ore than six years after the enactment of the Dodd-Frank Act, and more than three years after the US Commodity Futures Trading Commission (CFTC) required swap dealers to register in accordance with Title VII of that Act, it remains unclear when exactly the US Securities and Exchange Commission (SEC) will require the registration of security-based swap (SBS) dealers. But while the timing for registration is unclear, SBS dealing entities can now begin to take steps to facilitate their SEC registration.

Despite the SEC's progress in recent months in finalising its rules for SBS dealers – it has, among other things, recently issued amendments to its Regulation SBSR and finalised its business conduct rules for SBS dealers – several more dominoes need to fall before SBS dealer registration will be required. Of particular note, the SEC's SBS dealer registration rules provide that registration will not be required until at least six months after the publication in the Federal Register of the SEC's final margin rules for SBS dealers. The SEC proposed those rules in 2012 but, after that proposal, the Basel Committee on Banking Supervision and the International Organization of Securities Commissions released their widely influential international framework for margin for uncleared derivatives. As a result, it seems likely, though perhaps not inevitable, that the SEC will re-propose its margin rules. In view of that likely re-proposal, the required six-month waiting period after the final margin rules' publication, and SEC Chair Mary Jo White's recent statement at an open meeting that the SEC's goal is to complete its regulations for SBS dealers by the end of 2016, an SBS dealer registration compliance date toward the middle or end of 2017 seems likely.

Even if registration will not be required this year, the SBS rules that the SEC has created to date give a helpful if still somewhat inexact roadmap for registration by SBS dealers. What follows is a quick and non-exclusive list of action items for SBS dealing entities.

SBS dealers should consider their

internal division of labour for SBS processes and compliance. The bifurcated US regulatory scheme for derivatives means that dealers will need to run many processes in parallel. Those parallel processes, for CFTC-regulated swaps on the one hand, and for SEC-regulated SBS on the other, will in many cases be quite similar, but they will generally not be identical. Accordingly, a first-order question for dealers is to what extent they can and should use the same personnel and the same systems to comply with the parallel CFTC and SEC regulatory requirements.

Because SBS dealer registration is only required after an SBS dealing entity's trading activity exceeds an applicable *de minimis* threshold, many financial institutions that deal in SBS will wish to put in place processes to monitor the level of their SBS trading activity. SBS dealing institutions that do not intend to register as an SBS dealer should put in place processes to monitor the amount of their SBS dealing activity that counts toward the applicable *de minimis* thresholds, and should limit their trading activity so that it remains below those thresholds. Similarly, some institutions will likely wish to monitor their SBS dealing activity to determine when that activity exceeds a relevant threshold and requires SEC registration. Here, as in other areas, the CFTC and SEC rules are similar but not identical. One difference: although the SEC's phase-in *de minimis* threshold level for SBS that are credit default swaps is set at \$8 billion in notional amount over a 12-month period, the same as the CFTC's phase-in *de minimis* threshold level for swaps, the SEC's rules, unlike the CFTC's rules, also contain a separate *de minimis* threshold set at \$400 million, for SBS that are not credit default swaps.

## Registration

SBS dealing entities that intend to register with the SEC should begin preparations to provide the certifications that the SEC requires for registration. In one of those certifications, a senior officer of the applicant must certify that the applicant has developed and implemented written

policies and procedures reasonably designed to prevent violation of the federal securities laws and rules thereunder, and has documented the process by which they reached such determination. Accordingly, an SBS dealing entity should consider not only the range of the securities laws to which it is subject – apparently including laws that do not apply directly to SBS or SBS dealing activity – but also how it will document the process supporting the senior officer's certification that the applicant has implemented all required policies and procedures.

SBS dealers will also need to develop the policies and procedures, reasonably designed to prevent violation of the securities laws, as to which the senior officer will certify. Because of the many similarities between the SEC and CFTC rules, SBS dealers should in many cases be able to use their CFTC swap dealer policies as models for their SEC SBS dealer policies. At the same time, because the SEC and CFTC rules differ in many details, the new SBS dealer policies must be drafted carefully to reflect faithfully the SEC's requirements.

Additional considerations apply for non-resident SBS dealers, those that are incorporated, or have their principal place of business, outside of the United States. The SEC requires that such SBS dealers certify that they will, and that they provide an opinion of counsel stating that as a matter of law they can, provide the SEC with prompt access to books and records and submit to onsite SEC inspection and examination. Certain non-resident SBS dealers may find these requirements problematic under the laws of their home jurisdictions. In its registration rules release, the SEC goes so far as to suggest that certain SBS dealers may wish to consider restructuring their businesses to permit them to give this certification.

As the SEC continues to finalise its requirements for SBS dealers, additional considerations will undoubtedly arise. In the meantime, however, regardless of the exact timing for SBS dealer registration, there is no shortage of preparation that SBS dealing entities may begin to undertake.

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