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17 CFR Parts 240, 242, and 249
Registration and Regulation of Security-Based Swap Execution Facilities; Proposed Rule

SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 240, 242, and 249

[Release No. 34–63825; File No. S7–06–11]

RIN 3235–AK93

Registration and Regulation of Security-Based Swap Execution Facilities

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule; proposed interpretation.

SUMMARY: In accordance with Section 763 ("Section 763") of Title VII ("Title VII") of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank Act"), the Securities and Exchange Commission ("SEC" or "Commission") is proposing Regulation SB SEF under the Securities Exchange Act of 1934 ("Exchange Act") that is designed to create a registration framework for security-based swap execution facilities ("SB SEFs"); establish rules with respect to the Dodd-Frank Act's requirement that a SB SEF must comply with the fourteen enumerated core principles ("Core Principles") and enforce compliance with those principles; and implement a process for a SB SEF to submit to the Commission proposed changes to the SB SEF's rules. The Commission also is proposing an interpretation of the definition of "security-based swap execution facility" set forth in Section 3(a)(77) of the Exchange Act to provide guidance on the characteristics of those systems or platforms that would satisfy the statutory definition. In addition, the Commission is proposing to amend Rule 3a–1 under the Exchange Act to exempt a registered SB SEF from the Exchange Act's definition of "exchange" and to add Rule 15a–12 under the Exchange Act to exempt, subject to certain conditions, a registered SB SEF from regulation as a broker pursuant to Section 15(b) of the Exchange Act.

DATES: Comments should be submitted on or before April 4, 2011.

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 S7–06–11 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 in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F St., NE., Washington, DC 20549–1090.

All submissions should refer to File Number S7–06–11. 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 Web site (*http://www.sec.gov/rules/proposed.shtml*). Comments are also available for Web site viewing and printing in the Commission's Public Reference Room, 100 F St., NE., Washington, DC 20549 on official business days between the hours of 10 a.m. and 3 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.

FOR FURTHER INFORMATION CONTACT: Nancy J. Burke-Sanow, Assistant Director, at (202) 551–5621; David Liu, Senior Special Counsel, at (312) 353–6265; Constance Kiggins, Special Counsel, (202) 551–5701; Molly Kim, Special Counsel, at (202) 551–5644; Leah Mesfin, Special Counsel, at (202) 551–5655; Susie Cho, Special Counsel, at (202) 551–5639; Michou Nguyen, Special Counsel, (202) 551–5634; Heidi Pilpel, Special Counsel, (202) 551–5666; Steven Varholik, Special Counsel, at (202) 551–5615; Sarah Schandler, Special Counsel, at (202) 551–7145; and Iliana Lundblad, Attorney, at (202) 551–5871; Office of Market Supervision, Division of Trading and Markets, Securities and Exchange Commission, 100 F Street, NE., Washington, DC 20549–7010.

SUPPLEMENTARY INFORMATION: The Commission is proposing new Regulation SB SEF under the Exchange Act governing the registration and regulation of SB SEFs, an interpretation with respect to the definition of a SB SEF and new Form SB SEF for applicants to register with the Commission as SB SEFs. The Commission also is proposing certain exemptions to facilitate the trading of security-based swaps ("SB swaps") on SB SEFs.

I. Introduction

On July 21, 2010, the President signed the Dodd-Frank Act into law.[1] The Dodd-Frank Act was enacted, among other things, to promote the financial stability of the United States by improving accountability and transparency of the nation's financial system.[2] Title VII of the Dodd-Frank Act provides the Commission and the Commodity Futures Trading Commission ("CFTC") with the authority to regulate over-the-counter ("OTC") derivatives in light of the recent financial crisis, which demonstrated the need for enhanced regulation of the OTC derivatives market. The Dodd-Frank Act is intended to strengthen the existing regulatory structure concerning, and to provide the Commission and the CFTC with effective regulatory tools to oversee, the OTC swaps markets, which have grown exponentially in recent years and are capable of affecting significant sectors of the U.S. economy.

The Dodd-Frank Act provides that the CFTC will regulate "swaps," the Commission will regulate "security-based swaps," and the CFTC and the Commission will jointly regulate "mixed swaps."[3] The Dodd-Frank Act amends

[1] The Dodd-Frank Wall Street Reform and Consumer Protection Act (Pub. L. 111–203, H.R. 4173).

[2] *See* Public Law 111–203 Preamble.

[3] Section 712(d) of the Dodd-Frank Act provides that the Commission and the CFTC, in consultation with the Board of Governors of the Federal Reserve System ("Federal Reserve"), shall further define the terms "swap," "security-based swap," "swap dealer," "security-based swap dealer," "major swap participant," "major security-based swap participant," "eligible contract participant," and "security-based swap agreement." These terms are defined in Sections 721 and 761 of the Dodd-Frank Act and, with respect to the term "eligible contract participant," in Section 1a(18) of the Commodity Exchange Act ("CEA"), 7 U.S.C. 1a(18), as re-designated and amended by Section 721 of the Dodd-Frank Act. Further, Section 721(c) of the Dodd-Frank Act requires the CFTC to adopt a rule to further define the terms "swap," "swap dealer," "major swap participant," and "eligible contract participant" to include transactions and entities that have been structured to evade Title VII of the Dodd-Frank Act. Section 761(b) of the Dodd-Frank Act provides that the Commission may adopt a rule to further define the terms "security-based swap," "security-based swap dealer," "major security-based swap participant," and "eligible contract participant," with regard to security-based swaps, for the purpose of including transactions and entities that have been structured to evade Title VII of the Dodd-Frank Act. Finally, Section 712(a) of the Dodd-Frank Act provides that the Commission and CFTC, after consultation with the Federal Reserve, shall jointly prescribe regulations regarding "mixed swaps," as may be necessary to carry out the purposes of Title VII. To assist the Commission and the CFTC in further defining the terms specified above, and to prescribe regulations regarding "mixed swaps" as may be necessary to carry out the purposes of Title VII, the Commission and the CFTC have sought comment from interested parties. *See* Securities Exchange Act Release Nos. 63452 (December 7, 2010), 75 FR 80174 (December

the Exchange Act to require, among other things, the following with respect to transactions in SB swaps regulated by the Commission: (1) Transactions in SB swaps must be cleared through a clearing agency if they are of a type that the Commission determines must be cleared, unless an exemption from mandatory clearing applies;[4] (2) if the SB swap is subject to the clearing requirement, the transaction must be executed on an exchange or on a SB SEF registered under Section 3D of the Exchange Act or a SB SEF exempt from registration under Section 3D(e) of the Exchange Act, unless no SB SEF or exchange makes such SB swap available for trading or the SB swap transaction is subject to the clearing exception in Section 3C(g) of the Exchange Act;[5] and (3) transactions in SB swaps (whether cleared or uncleared) must be reported to a registered security-based swap data repository ("SDR") or the Commission.[6]

II. Regulatory Framework of Security-Based Swap Execution Facilities

Currently, SB swaps trade in the OTC market, rather than on regulated markets. Although some SB swaps have moved to centralized clearing, prior to the enactment of the Dodd-Frank Act, centralized clearing of SB swaps was not required. The current market for SB swaps is opaque, with little, if any, pre-trade transparency (the ability of market participants to see trading interest prior to a trade being executed) or post-trade transparency (the ability of market participants to see transaction information after a trade is executed). A key goal of the Dodd-Frank Act is to bring trading of SB swaps onto regulated markets,[7] as reflected in the statutory requirement that, subject to certain exceptions, any SB swap subject to mandatory clearing must be traded on a SB SEF or an exchange, unless no SB SEF or exchange makes such SB swap available for trading.

Section 763 of the Dodd-Frank Act amends the Exchange Act by adding various new statutory provisions to govern the regulation of SB SEFs.[8] Section 3C(h) of the Exchange Act specifies that transactions in SB swaps that are subject to the clearing requirement of Section 3C(a)(1) of the Exchange Act must be executed on an exchange or on a SB SEF registered with the Commission (or a SB SEF exempt from registration), unless no exchange or SB SEF makes the SB swap available to trade (referred to as the "mandatory trade execution requirement") or the SB swap transaction is subject to the clearing exception in Section 3C(g) of the Exchange Act ("end-user exception").[9] Further, Section 3D(a)(1) of the Exchange Act states that no person may operate a facility for the trading or processing of SB swaps, unless the facility is registered as a SB SEF or as a national securities exchange under that section.[10] Under Section 3D(b) of the Exchange Act, a SB SEF registered with the Commission may make SB swaps available for trading and facilitate trade processing of SB swaps.[11] Section 3D(c) of the Exchange Act requires a national securities exchange, to the extent it also operates a SB SEF and uses the same electronic trade execution system for listing and executing trades in SB swaps, to identify whether electronic trading of SB swaps is taking place on or through the exchange or the SB SEF.[12]

Section 3D(d) of the Exchange Act specifies that to be registered and maintain registration, a SB SEF must comply with fourteen Core Principles enumerated therein and any requirement that the Commission may impose by rule or regulation.[13] The Core Principles applicable to SB SEFs are captioned: (1) Compliance with Core Principles; (2) Compliance with Rules; (3) Security-Based Swaps Not Readily Susceptible to Manipulation; (4) Monitoring of Trading and Trade Processing; (5) Ability to Obtain Information; (6) Financial Integrity of Transactions; (7) Emergency Authority; (8) Timely Publication of Trading Information; (9) Recordkeeping and Reporting; (10) Antitrust Considerations; (11) Conflicts of Interest; (12) Financial Resources; (13) System Safeguards; and (14) Designation of Chief Compliance Officer.[14] As a result, a registered SB SEF would have certain regulatory obligations with respect to overseeing its market and the participants that trade on its facility. Further, Section 3D(f) of the Exchange Act states that the Commission shall prescribe rules governing the regulation of SB SEFs.[15] Finally, Section 3(a)(77) of the Exchange Act defines a SB SEF as a trading system or platform in which multiple participants have the ability to execute or trade SB 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: (1) Facilitates the execution of SB swaps between persons; and (2) is not a national securities exchange.[16]

As regulated markets for the trading of SB swaps, SB SEFs, as well as exchanges that post or trade SB swaps ("SBS exchanges"), are intended to play an important role in enhancing the transparency and oversight of the market for SB swaps. SB SEFs should help further the statutory objective of greater transparency and a more competitive environment for the trading of SB swaps by providing a venue for multiple parties to execute trades in SB swaps and also by serving as a conduit for information regarding trading interest in SB swaps. As a result of the Dodd-Frank Act's provisions relating to SB SEFs, the Commission would have access to information on the trading of SB swaps that occurs on SB SEFs and information regarding trading by their participants. In addition, because SB SEFs would have certain regulatory obligations arising from their Core

21, 2010) (File No. S7–39–10) (proposed rulemaking regarding definitions contained in Title VII of the Dodd-Frank Act relating to participants). The Commission also will propose rules regarding definitions contained in Title VII of the Dodd-Frank Act relating to products in a separate proposed rulemaking. *See also* Securities Exchange Act Release No. 62717 (August 13, 2010), 75 FR 51429 (August 20, 2010) (File No. S7–16–10) (advance joint notice of proposed rulemaking regarding definitions contained in Title VII of the Dodd-Frank Act).

[4] *See* Public Law 111–203, § 763(a) (adding Section 3C(a)(1) of the Exchange Act).

[5] *See* Public Law 111–203, § 763(a) (adding Section 3C(h) of the Exchange Act). *See also* Public Law 111–203, § 761(a) (adding Section 3(a)(77) of the Exchange Act), defining the term "security-based swap execution facility." The Dodd-Frank Act amends the CEA to provide for a similar regulatory framework with respect to transactions in swaps regulated by the CFTC.

[6] *See* Public Law 111–203, § 761(a)(75) (adding Section 3(a)(75) of the Exchange Act) (defining the term "security-based swap data repository"). The registration of an SDR and the reporting of SB swaps are the subject of separate Commission rulemakings. *See* Securities Exchange Act Release Nos. 63347 (November 19, 2010), 75 FR 77306 (December 10, 2010) (File No. S7–35–10) ("SDR Release") and 63346 (November 19, 2010), 75 FR 75208 (December 2, 2010) (File No. S7–34–10) ("Reporting and Dissemination Release").

[7] *See* Public Law 111–203, preamble.

[8] *See* Public Law 111–203, § 763 (adding Sections 3C and 3D of the Exchange Act).

[9] *See* Public Law 111–203, § 763 (adding Section 3C(h) of the Exchange Act).

[10] *See* Public Law 111–203, § 763(a) (adding Section 3D(a)(1) of the Exchange Act). The Commission views this requirement as applying only to facilities that meet the definition of "security-based swap execution facility" in Section 3(a)(77) under the Exchange Act. SB swaps that are not subject to the mandatory trade execution requirement would not have to be traded on a registered SB SEF and could be traded in the over-the-counter ("OTC") market for SB swaps.

[11] *See* Public Law 111–203, § 763(c) (adding Section 3D(b) of the Exchange Act).

[12] *See* Public Law 111–203, § 763(c) (adding Section 3D(c) of the Exchange Act).

[13] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(1)(A) of the Exchange Act).

[14] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(1)–(14) of the Exchange Act).

[15] *See* Public Law 111–203, § 763(c) (adding Section 3D(f) of the Exchange Act).

[16] *See* Public Law 111–203, § 761(a) (adding Section 3(a)(77) of the Exchange Act).

Principles, such as monitoring trading, assuring the ability to obtain information, and establishing and enforcing rules and procedures to ensure the financial integrity of SB swaps entered on or though the SB SEF, these facilities can play an important role in helping to oversee the market for SB swaps on an ongoing basis and allowing regulators to quickly assess information regarding the potential for systemic risk across trading venues.

The Commission is mindful that any rules that the Commission may adopt regarding the regulation of SB SEFs could impact the incentives for existing or prospective platforms for the trading of SB swaps to enter or withdraw from this market. On the other hand, the rules to be adopted by the Commission for the trading of SB swaps should be sufficient to fulfill the objectives of the Dodd-Frank Act to promote financial stability and transparency. The Commission also is mindful that, both over time and as a result of Commission proposals to implement the Dodd-Frank Act, the further development of the SB swap market may alter some of the specific calculus for future regulation of SB SEFs.

The Commission notes that the CFTC is proposing rules relating to swap execution facilities ("SEFs") as required under Section 733 of the Dodd-Frank Act.[17] Because there are differences between the markets and products that the Commission and the CFTC currently regulate, the approach that each agency may take regarding the regulation of SB SEFs and SEFs, respectively, also may differ in various respects. The Commission recognizes that commenters may respond to the Commission's proposals by referring to the CFTC's proposals and welcomes commenters' views and suggestions on the impact of any differences between the Commission and CFTC approaches to the regulation of SB SEFS and SEFs. The Commission is particularly interested in whether its proposed rulemaking would result in any duplicative or inconsistent efforts on the part of market participants subject to both regulatory regimes or would result in gaps between those regimes.

Further, the Commission is aware that regulators in other countries are considering reform of their swaps and derivatives markets and are interested in achieving a consistent approach to swaps regulation between the United States, Europe and other jurisdictions to mitigate the risk of regulatory arbitrage.[18] Although the Commission must be guided by the requirements of the Dodd-Frank Act in crafting proposed rules applicable to markets that trade SB swaps and the participants in those markets, the Commission recognizes that the particular rules that it may adopt under the Dodd-Frank Act may impact the incentives of market participants with respect to where they choose to engage in the trading of SB swaps.

Commenters are urged to consider generally the role that regulation may play in fostering or limiting the development of the market for SB swaps (or, vice versa, the role that market developments may play in changing the nature and implications of regulation) and specifically to focus on this issue with respect to the proposals to establish a framework for the trading of SB swaps. In addition, commenters are urged to consider the effect of the Commission's proposals relating to SB SEFs on the global swaps and derivatives markets and to offer specific comments regarding how the proposals compare with the existing or proposed regulations of other jurisdictions.

III. The Definition of Security-Based Swap Execution Facilities

Since the enactment of the Dodd-Frank Act in July 2010, the Commission has engaged in a number of outreach programs relating to the legislation's rulemaking mandates, including trading of SB swaps on regulated markets.[19] On September 15, 2010, the staff of the Commission and of the CFTC conducted a joint roundtable to discuss issues related to the formation and regulation of SEFs and SB SEFs ("Roundtable").[20] Topics discussed at the Roundtable included the scope of the definition of a SEF and SB SEF; registration of these facilities; products that would trade on a SEF and SB SEF; block trades; access to SEFs and SB SEFs; and cross-market issues.[21] The purpose of the Roundtable was to provide a forum for the discussion of these issues and to assist SEC and CFTC staff as they developed proposed rules to meet the Dodd-Frank Act's mandate to bring the trading of swaps and SB swaps subject to the mandatory clearing requirement onto organized markets. Panelists at the Roundtable provided comments on their experience with the current market structure for the trading of swaps and SB swaps and offered their views and suggestions on ways that that structure could change as a result of the legislation. Pursuant to the Commission's outreach, a range of individuals and entities, including swap dealers, brokers, end-users, academics and others, have expressed their views on a variety of topics, such as the scope of activities or the nature of platforms that should fall within the statutory definition of "security-based swap execution facility."[22]

Many letters from market participants advocated for a flexible interpretation of the statutory definition of SB SEF.[23] In their letters, they argued that the definition of SB SEF should permit many different types of existing and new trading and execution platforms.[24] Certain market participants noted that the SB swap market is more customized and illiquid than the cash equities market and argued that a broad range of trading models would be necessary to address the SB swap market's unique characteristics and to allow this market to develop properly.[25]

[17] *See* Public Law 111–203, § 733 (adding Section 5h of the CEA). *See also* 76 FR 1214 (January 7, 2011) ("Notice of proposed SEF rulemaking by the CFTC").

[18] *See, e.g.,* Committee of European Securities Regulators ("CESR"), CESR Technical Advice to the European Commission in the context of the MiFID Review and Responses to the European Commission for Additional Information, dated October 13, 2010, available at *http://www.cesr-eu.org/index.php ?page=contenu_groups&id=61&docmore=1.*

[19] *See, e.g.,* Implementing the Dodd-Frank Wall Street Reform and Consumer Protection Act, Transparency, Public Input on SEC Regulatory Initiatives under the Dodd-Frank Act Title VII—Wall Street Transparency and Accountability, Mandatory Exchange Trading and Swap Execution Facilities, available at *http://www.sec.gov/spotlight/dodd-frank.shtml.*

[20] *See* Securities Exchange Release No. 62864 (September 8, 2010), 75 FR 55574 (September 13, 2010) (File No. 4–612). Webcast available at *http:// www.sec.gov/news/openmeetings/2010/ jac091510.shtml.*

[21] *See* Press Release issued by the Commission on September 8, 2010, "SEC, CFTC To Host Joint September Roundtables On Swap and Security-Based Swap Matters" (File No. 2010–166), available at *http://www.sec.gov/news/press/2010/2010-166.htm.*

[22] *See, e.g., http://www.sec.gov/spotlight/dodd-frank.shtml.*

[23] *See, e.g.,* letter from Ben Macdonald, Global Head Fixed Income, Bloomberg LP, to Commission, dated September 22, 2010 ("Bloomberg Letter"), at 2; letter from Richard H. Baker, President and CEO, Managed Funds Association, to Elizabeth M. Murphy, Secretary, Commission, dated September 22, 2010 ("MFA Letter"), at 16; letter from Ernest C. Goodrich, Jr., Managing Director—Legal Department, and Marcelo Riffaud, Managing Director—Legal Department, Deutsche Bank AG, to David A. Stawick, Secretary, CFTC, and Elizabeth M. Murphy, Secretary, Commission, dated October 6, 2010 ("Deutsche Bank Letter"), at 5–6 and 8–9; and letter from Larry Tabb, CEO and Founder, Andy Nybo, Head of Derivatives, and Kevin C. McPartland, Senior Analyst, TABB Group, to Gary Gensler, Chairman, CFTC, and Mary Schapiro, Chairman, Commission, dated August 23, 2010 ("TABB Letter"), at 2.

[24] *See, e.g.,* Bloomberg Letter, *id.,* at 2; MFA Letter, *id.,* at 16; and Deutsche Bank Letter, *id.,* at 7.

[25] *See, e.g.,* Bloomberg Letter, *supra* note 23, at 2, and Deutsche Bank Letter, *supra* note 23, at 6–7. *See also infra,* Section III.B for a discussion of the

Although many commenters who expressed a view regarding the definition of SB SEF favored allowing multiple platforms,[26] some commenters expressed concern about some types of platforms that potentially could meet the definition of SB SEF. One commenter believed that allowing multiple request for quote ("RFQ") platforms,[27] without a price mechanism that aggregates prices across platforms, to meet the definition of SB SEF, could lead to a fragmented market, which could discourage competition.[28] Another commenter suggested that permitting an RFQ platform to be treated as a SB SEF could be viewed as preserving the *status quo* of a dealer-dominated market and believed that the Dodd-Frank Act envisioned that SB swaps would be traded on a facility akin to a limit order book platform.[29]

The Commission also received other specific views about platforms that commenters believed should or should not be included in the definition of SB SEF. For example, one commenter believed that platforms that would not trade or execute SB swap transactions, such as pure trade processing facilities, would not meet the statutory definition of SB SEF.[30] A market participant, however, stated that in its view the statutory definition of SB SEF would encompass pure trade processing facilities.[31]

The information presented at the Roundtable and received from the public has helped to inform the proposals relating to SB SEFs that are part of this rulemaking. The Commission is mindful that there exists a wide range of views on the part of market participants and others about the nature of the activities or systems that would constitute, and the scope of activities permitted by, a SB SEF and therefore encourages interested persons to provide their views and suggestions, as well as any materials or data to support their positions, on this aspect of the proposed rulemaking. The Commission believes that the prudent course is to take where appropriate a deliberate and attentive approach to its regulation of SB SEFs that is informed by the state of development of SB swap trading on regulated markets. The Commission emphasizes, however, that any actions it may take now or in the future would be designed to further the overall objectives of the Dodd-Frank Act.

A. Current SB Swap Market

1. Trading Models

Unlike the markets for cash equity securities and listed options, the market for SB swaps currently is characterized by bilateral negotiation in the OTC swap market; is largely decentralized; many instruments are not standardized; and many SB swaps are not centrally cleared. The lack of uniform rules concerning the trading of SB swaps and the one-to-one nature of trade negotiation in SB swaps has resulted in the formation of distinct types of venues for the trading of these securities, ranging from bilateral negotiations carried out over the telephone, to single-dealer RFQ platforms, to multi-dealer RFQ platforms, to central limit order books outside the United States, and others, as more fully described below. The use of electronic media to execute transactions in SB swaps varies greatly across trading venues, with some venues being highly electronic whereas others rely almost exclusively on non-electronic means such as the telephone. The reasons for use of, or lack of use of, electronic media vary from such factors as user preference to limitations in the existing infrastructure of certain trading platforms. The description below of the ways in which SB swaps may be traded is based in part on discussions with market participants. The Commission solicits comments on the accuracy of this description.

The Commission uses the term "bilateral negotiation" to refer to the model whereby one party uses the telephone, e-mail or other communications to contact directly a potential counterparty to negotiate a SB swap. Once the terms are agreed, the SB swap transaction is executed and the terms are memorialized.[32] In a bilateral negotiation, there may be no pre-trade or post-trade transparency available to the marketplace because only the two parties to the transaction are aware of the terms of the negotiation and the final terms of the agreement. Further, no terms of the proposed transaction are firm until the transaction is executed. However, reputational costs generally serve as a deterrent to either party's failing to honor any quoted terms. Dealer to customer bilateral negotiation currently is used for all SB swap asset classes, and particularly for trading in less liquid SB swaps, in situations where the parties prefer a privately negotiated transaction, such as in executing block trades, or in other circumstances in which it is not cost effective for a party to the trade to use one of the execution methods described below.

Another model for the trading of SB swaps is the single-dealer RFQ electronic trading platform. In a single-dealer RFQ platform, a dealer may post indicative quotes for SB swaps in various SB swap 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 SB swap, the customer requests an executable quote, the dealer provides one, and if customer accepts the dealer's quote, the transaction is executed electronically. If the dealer repeatedly responds to requests for executable quotes with quotes that are significantly less favorable than the dealer's indicative quotes posted on the single-dealer electronic trading platform, volume on the platform presumably would diminish and participants may no longer transact there. 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. Currently, there is no post-trade reporting of transactions on single-dealer platforms and thus there is no post-trade transparency.

A variant of the single-dealer model is an aggregator-type platform that combines two or more single-dealer RFQ platforms. In such a platform, a customer who has access to the platform, which is determined solely at the discretion of its operator and of the dealers involved, may see indicative quotes from multiple dealers at once instead of seeing quotes only from one

Commission's interpretation of the definition of SB SEF.

[26] *See supra* note 23 and accompanying text.

[27] In referring to a RFQ platform, the Commission means a trading platform where a customer who wishes to execute a SB swap disseminates a request for quote to one or more dealers and one or more of those dealers respond to the request with an executable quote.

[28] *See, e.g.,* Commentary by S. "Vish" Viswanathan, Professor, Fuqua School of Business, Duke University, at the Roundtable. Webcast available at *http://www.sec.gov/news/openmeetings/2010/jac091510.shtml.*

[29] *See* Commentary by Heather Slavkin, Senior Legal Policy Advisor for the Office of Investment, AFL–CIO, at the Roundtable. Webcast available at *http://www.sec.gov/news/openmeetings/2010/jac091510.shtml. See also infra,* Section III.B discussing the Commission's interpretation taking into account concerns raised by commenters.

[30] *See* letter from Mark D. Young, Skadden, Arps, Slate, Meagher & Flom LLP, to David A. Stawick, Secretary, CFTC, and Elizabeth M. Murphy, Secretary, Commission, dated September 22, 2010, at 3.

[31] *See* Meetings with SEC Officials: Memorandum from the Division of Trading and Markets regarding an August 25, 2010 Meeting with representatives of MarkitSERV, dated September 2, 2010, MarkitSERV PowerPoint Presentation, dated August 25, 2010 at p. 5–6, available at *http://www.sec.gov/comments/s7-16-10/s71610-96.pdf.*

[32] For further discussion, *see, e.g.,* Securities Exchange Act Release No. 63727 (January 14, 2011), 76 FR 3859 (January 21, 2011) (proposing rules for the trade acknowledgement and verification of security-based swaps).

dealer as in the single-dealer RFQ platform. Although a participant can simultaneously view quotes from multiple dealers, the participant can request a firm quote from only one dealer at a time. One feature of the aggregated single-dealer platform as compared to the bilateral negotiation and single-dealer models described above is the ability of a participant in the aggregated single-dealer platform to see indicative quotes from multiple dealers. However, customers are not afforded an opportunity to send RFQs to multiple dealers at the same time to promote competitive pricing. Also, like the single-dealer electronic platform, there is no post-trade reporting of transactions and thus there is no post-trade transparency.

A third model is the multi-dealer RFQ electronic trading platform.[33] In a multi-dealer RFQ system, a requester can send an RFQ to solicit quotes on a certain SB swap from multiple dealers at the same time. Currently, dealers on a multi-dealer RFQ platform generally require the platform to set limits on the number of dealers to whom a customer may send an RFQ, and also may limit which dealers may participate on the platform. These platforms are sometimes owned by dealers themselves. 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. But to the extent that a requester is restricted by platform rules to soliciting quotes from a limited number of dealers, the customer's pre-trade transparency is restricted to that number of quotes it receives in response to its RFQ. In some instances requestors may prefer to limit the number of recipients of an RFQ as a way to protect proprietary trading strategies as dissemination of their interest to multiple dealers may increase hedging costs to dealers, and thus costs to the requestors as reflected in the prices from the dealers. Pre-trade transparency may also exist through the platform's dissemination of composite indicative quotes to all participants prior to trades. Post-trade transparency may exist if the platform chooses to disseminate information regarding executed transactions.

A fourth model for the trading of SB swaps is a limit order book system or similar system, which the Commission understands is not yet in operation for the trading of SB swaps in the United States but exists for the trading of SB swaps in Europe. Today, securities and futures exchanges in the United States display a limit order book 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. A limit order book system may be a more suitable model for the trading of more liquid, rather than less liquid, SB swaps. In general, a limit order book system also provides greater pre-trade transparency than the three platforms described above because all participants can view bids and offers before placing their bids and offers. However, broadly communicating trading interest, particularly about a large trade, may increase hedging costs, and thus costs to investors as reflected in the prices from the dealers. The system can also provide post-trade transparency, to the extent that participants can see the terms of executed transactions.

A fifth type of trading, which the Commission herein refers to as "brokerage trading," is used by brokers to execute SB swap trades on behalf of customers, often in larger sized transactions. In such a system, a broker receives a request from a customer (which may be a dealer) who seeks to execute a specific type of SB swap. The broker then interacts with other customers to fill the request and execute the transaction. The mode of interaction can vary depending on the size of the trade and the type of SB swap being traded. In some cases, the interaction is done purely by voice over the telephone, while in other cases, the interaction is electronic or a hybrid of voice and an electronic system. The level of automation and use of electronic means also vary depending on the technological state and functionality of the broker's platform.[34] This model often is used by dealers that seek to transact with other dealers through the use of an interdealer 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 and post-trade transparency to the extent that participants can see the terms of executed transactions.

The five foregoing examples represent broadly the various types of models for the trading of OTC swaps in existence today. These examples may not represent every single method in existence today and the discussion above is intended to give an overview of the models without providing the nuances of each particular type.

2. The SB Swap Market and the Commission's Approach to SB SEF Definitions

In the Commission's view, the diverse nature of these examples demonstrates the extent to which, when compared with the equities markets, certain aspects of the SB swap market are still evolving.[35] In considering ways in which the Commission could approach the definition of SB SEF, the Commission has sought to facilitate competition and innovations in the SB swap market that could be used to promote more efficient trading in organized, transparent and regulated trading venues. The Commission does not believe it should simply overlay the same regulatory structure that is currently in place for equities, given important differences in the nature and maturity of the SB swap and equities markets. However, the Commission does believe that certain elements of equity

[33] The single-dealer RFQ platform is an example of a system that permits customers to submit an RFQ to a single dealer, which is distinct from a multi-dealer RFQ platform that permits customers to solicit quotes from multiple dealers simultaneously instead of one dealer. The multi-dealer RFQ platform differs from a single-dealer aggregator platform because a participant in the aggregated single-dealer platform may only send a request to one dealer at a time and thus would not have the ability to interact with the bids or offers of multiple dealers simultaneously.

[34] The Commission understands that a small portion of the brokerage trading in the United States is currently highly automated and has characteristics of a limit order book. However, while depth of the order book may be displayed, generally there may be only one bid or offer, and sometimes only one side of the market would be displayed (*i.e.,* a bid without an offer and vice versa). Because the volume in some SB swaps may be low, the electronic systems maintained by wholesale brokers would not necessarily include a matching engine that would provide for price-time priority or other execution parameters, unlike other types of electronic limit order books. Although the wholesale brokers' systems are electronic, the customer would need to perform some steps manually (*e.g.,* hit the bid or lift the offer) to execute a trade.

[35] For example, data from the Depository Trust and Clearing Corporation covering the period from March 22, 2010 to June 20, 2010 for single name credit default swaps revealed the following: Out of 998 types of swaps (*i.e.,* a swap based on one reference entity), only 55 had 10 or more trades per day (34 trades being the highest), and 827 of the swaps had 5 or fewer trades per day (531 of those only had 2 or fewer trades per day). In the data set, "trades per day" includes all tenors (*e.g.,* duration or expiry) in swaps of the same reference entity. *See http://www.dtcc.com/downloads/products/derivserv/CDS_Snapshot_Analysis_Sep17-2010.pdf; see also http://www.dtcc.com/products/derivserv/data_table_snap0002.php* and *http://www.dtcc.com/products/deriserv/data_table_snapshot.php.*

market structure may be directly relevant to the SB swap market.

Furthermore, rather than proposing a rule that would establish a prescribed configuration for SB SEFs that would meet the statutory definition of SB SEF, the Commission proposes to provide baseline principles interpreting the definition of SB SEF, consistent with the requirements of the Exchange Act, as amended by the Dodd-Frank Act, which any entity would need to be able to meet to register as a SB SEF. Such an approach is designed to allow flexibility to those trading venues that seek to register with the Commission as a SB SEF and to permit the continued development of organized markets for the trading of SB swaps. This more flexible approach also would allow the Commission to monitor the market for SB swaps and propose adjustments, as necessary, to any interpretation that it may adopt as this market sector continues to evolve.

However, the Commission recognizes that, consistent with the Dodd-Frank Act, the interpretation of the definition of SB SEF should: (1) Encourage the migration of trading SB swaps from the OTC market to SB SEFs (or exchanges), (2) provide a meaningful distinction between a SB SEF and an OTC trading venue, (3) promote further transparency of the SB swap market, and (4) to facilitate competition and innovation in the SB swap markets that could be used to promote more efficient trading in organized, transparent, and regulated trading venues. In addition, the interpretation of the definition of SB SEF should complement other aspects of proposed SB swap regulations, including those related to post trade transparency, mandatory clearing, and the general requirement that SB swaps that are subject to mandatory clearing only be traded on an exchange or SB SEF, unless no exchange or SB SEF makes the SB swap available to trade.

B. Scope of SB SEF Definition

As noted above, Section 3(a)(77) of the Exchange Act defines a SB SEF as a trading system or platform in which multiple participants have the ability to execute or trade SB 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: (1) Facilitates the execution of SB swaps between persons; and (2) is not a national securities exchange.[36]

A key issue noted at the Roundtable and raised by market participants generally regarding Dodd-Frank Act implementation is the scope of the definition of "security-based swap execution facility."[37] SB swap industry participants have expressed an interest in, and offered their views on, the parameters of the definition of SB SEF.[38] Such participants asserted that the interpretation of the definition of SB SEF is a significant issue for the SB swap industry because, under the mandatory trade execution requirement in Section 3C(h) of the Exchange Act, a SB swap subject to mandatory clearing must be executed on a SB SEF or on an exchange, if made available for trading. The discussion below sets forth the Commission's preliminary view as to the meaning of the various elements of this definition.

The "multiple participant to multiple participant" requirement in the definition of SB SEF prescribes that "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."[39] Consistent with this requirement, the Commission proposes to interpret the definition of SB SEF to mean a system or platform that allows more than one participant to interact with the trading interest of more than one other participant on that system or platform. The Commission notes that this definition can be satisfied by various types of platforms, but some platforms that are currently used to trade SB swaps in the OTC market would not meet this definition, and would not be considered SB SEFs. As noted above, the Commission is aware that the movement of SB swaps trading onto regulated platforms is still in an emergent stage. Therefore, in considering ways in which the Commission could approach the definition of SB SEF, the Commission has sought to facilitate competition and innovations in the SB swaps market that could be used to promote more efficient trading in organized, transparent and regulated trading venues to support the Dodd-Frank Act's goal of moving the trading of SB swaps onto regulated markets.

Under this proposed interpretation, if a system or platform were to allow an individual participant (of which there must be more than one on the system, but which do not need to be acting simultaneously) to send, at the same time, a single RFQ to all other liquidity providing participants on that system or platform and view responses from those participants, the Commission believes that such a model would satisfy the requirements of the statutory definition, even if the quote requesting participants are acting at different times. A key element to this model is that the SB SEF would not be able to limit the number of liquidity providing participants from whom a participant could request a quote on the SB SEF.[40]

The Commission further believes that the requirements of the statutory definition would be met if the system or platform not only provided the quote requesting participant with the ability to send a single RFQ to all liquidity providing participants, but also provided the quote requesting participant with the ability to choose to send an RFQ to fewer than all liquidity providing participants. In the Commission's view, a system or platform that affords a quote requesting participant the ability to send an RFQ to all participants, but also permits the quote requesting participant to choose to send an RFQ to fewer participants, would satisfy the statutory definition because multiple participants would have *the ability* to execute or trade SB swaps by accepting bids or offers made by multiple participants. The person exercising investment discretion for the transaction, whether it is the participant itself or the participant's customer, would be the person that would have the ability to choose to send the RFQ to less than all participants, as they would be in the best position to determine the impact on their interest of a broad or narrow dissemination of their RFQ.[41]

Under the proposed interpretation of the definition of SB SEF, a SB SEF would be able to offer functionality to a participant (or a participant's customer) enabling that participant to choose to send a single RFQ to any number of specific liquidity providing participants on the SB SEF, including just a single liquidity provider. The

[36] As discussed *infra* Section XXI, an entity that meets the definition of SB SEF would be required to register as a SB SEF or a national securities exchange (unless exempted under Section 3D(e) of the Exchange Act if the Commission finds that the facility is subject to comparable, comprehensive supervision and regulation on a consolidated basis by the CFTC). A registered SB SEF would be required to satisfy all 14 Core Principles and any rules promulgated by the Commission, including proposed Rule 811(a)(3), which provides for certain requirements relating trading on a SB SEF. *See* Public Law 111–203, § 763(c) (adding Section 3D(a)(1) and (d)(1) of the Exchange Act).

[37] *See, e.g.,* Bloomberg Letter, *supra* note 23, at 2, and MFA Letter, *supra* note 23, at 16.

[38] *See supra* notes 23 to 25.

[39] *See* Public Law 111–203, § 763(a) (adding Section 3(77) of the Exchange Act).

[40] *See infra* Section VIII.C.

[41] Regardless of the number of participants to which a RFQ was sent, the response(s) to that RFQ would be required to be included in the composite indicative quote of the SB SEF. *See infra* note 152 and accompanying text.

Commission requests comment on whether in addition to providing this flexibility to investors initiating RFQs, the interpretation should also set a floor for the minimum number of liquidity providers that must be included in an RFQ (and, if so, what that minimum number should be). Commenters should be mindful that in proposing its interpretation of the definition of SB SEF, the Commission is trying to balance the above-stated goal of encouraging SB swap trading to move onto regulated markets with the goal of promoting greater transparency in the trading of SB swaps.

On the one hand, providing investors as much choice as possible in determining how to route an RFQ on a SB SEF may incentivize investors to trade on a SB SEF when they otherwise might not have made that choice. Since those investors that have a fiduciary duty must seek best execution for a transaction, they may have a natural incentive to route to multiple dealers. However, this incentive may be impacted by the liquidity characteristics of the SB swap. Market participants, including dealers and buy-side customers, have raised concerns regarding pre-trade transparency of SB swap trades, particularly block trades. They believe that if other market participants know the terms of a trade prior to the time it is executed, those other market participants could attempt to profit from the information about the trade to the detriment of the initiator of the trade.[42] Therefore, particularly for illiquid SB swaps, an investor may determine that it is in its best interest not to broadly project its trading intention, and may choose to send a RFQ to one dealer.[43] Other investors could still benefit by the request because the response to that RFQ would become part of the composite indicative quote of that SB SEF.[44] Providing investors the choice to send a RFQ to only one dealer on a SB SEF—as long as they have the ability to send it to more than one if they chose to—may encourage investors to execute trades on a SB SEF even with respect to SB swaps that are not required to be traded on a SB SEF or an exchange, thus supporting the development of trading on regulated platforms and venues in the United States, rather than in other jurisdictions.

On the other hand, requiring that all RFQs on a SB SEF be sent to more than one dealer could force competition among dealers more than if RFQs to a single dealer were permitted. This competition may lead to lower spreads as dealers compete with each other on price. Further, this competition may provide for a more robust composite indicative quote because a greater number of responses would be incorporated into the composite. In addition, requiring that RFQs be sent to more than one dealer provides for the possibility that a response from a dealer other than the one with whom the investor may have "pre-arranged" the transaction will result in a better price. However, market participants have expressed a concern that requiring a broad level of pre-trade transparency, particularly for illiquid products, may not lead to better prices and in certain circumstances may lead to worse prices provided by dealers if dealer hedging is made more difficult after the intent to trade has been projected to the entire market.

In addition, the Commission proposes to interpret the statutory requirement that "multiple participants have the ability to execute or trade SB swaps by accepting bids and offers made by multiple participants in the facility or system" to require a SB SEF to provide at least a basic functionality to allow any participant on the SB SEF the ability to make and display executable bids or offers accessible to all other participants on the SB SEF, if the participant chooses to do so. The Commission preliminarily believes that such a requirement would allow for increased price transparency beyond what would be found in the bilateral OTC market, if a market participant chooses to utilize the functionality to display a bid or offer.

Under the proposed interpretation of the definition of SB SEF (either with or without the additional requirement for a minimum number of liquidity providers to be included in every RFQ), the traditional bilateral negotiation model, as described above, would not fall within the definition of SB SEF because there would be only one party able to seek a quote and only one party that is able to provide a quote in response. The Commission believes that the inclusion of the phrase "through any means of interstate commerce" in the definition of SB SEF would not, by itself, support the proposition that bilateral negotiation would satisfy the definition's terms; the trading system or platform would still need to meet the other requirements of the definition, specifically, the requirement that multiple participants have the ability to execute or trade SB swaps by accepting bids and offers made by multiple participants in the facility or system ("multiple participant to multiple participant requirement").

Likewise, a platform where there is a single dealer interacting with multiple customers on the other side of the transaction would not appear to meet the "multiple participant to multiple participant" requirement because the dealer is only one person. This would be true for aggregated single-dealer platforms as well, because a participant on such a platform may only submit one request at a time and receive only one response at a time, on a dealer-by-dealer basis.

The Commission proposes that the definition of SB SEF cannot be satisfied by the simple aggregation of trading interest across trading systems or platforms to meet the "multiple participant to multiple participant" requirement. That is, each trading method—when viewed in isolation—would need to individually meet the "multiple participant to multiple participant" requirement on its own. Thus, an entity that relies on a bilateral negotiation system with one participant on each end of the telephone or similar communication system, but with several such conversations occurring simultaneously, could not claim to meet the definition of SB SEF by asserting that when those conversations are viewed in the aggregate, *i.e.,* bilateral negotiation between persons A and B to facilitate one transaction, and bilateral negotiation between persons C and D, to facilitate a separate transaction, that the "multiple participant to multiple participant" requirement is met.[45] Two independent single-dealer platforms also may not be construed in the aggregate in order to meet the "multiple participant to multiple participant" requirement. In each of these situations, there is no opportunity for interaction among participants, except on a "one participant to one participant" basis.

However, a system or platform that provides for an auction for a class of SB swaps to be held at a prescribed time and that allows multiple participants to interact with each other, with trades executed pursuant to a pre-determined algorithm, could meet the proposed interpretation of the definition of SB SEF. In addition, the Commission believes that a limit order book system as described above for the trading of SB swaps could satisfy the proposed interpretation of the definition of SB

[42] *See* discussion in Section VIII.C and D *infra.*

[43] *See* Reporting and Dissemination Release, *supra* note 6, at 89–93.

[44] *See* discussion of proposed Rule 811(d)(5) in Section VIII.C *infra.*

[45] However, as discussed further below in the discussion of the application of the definition of SB SEF to wholesale brokers, if person A negotiates with persons B, C and D as part of the same transaction, the "multiple participant to multiple participant" requirements may be able to be met. *See infra* note 46 and accompanying text.

SEF. Such a model generally would allow interaction between multiple (*i.e.,* two or more) firm orders or bids and offers. Moreover, to satisfy the definition of SB SEF, a system or platform would not need to be limited to only one type of trading model. An entity that wishes to register as a SB SEF could operate different trading models for different SB swap products, as long as each trading system or platform on its own meets the interpretation of the definition of SB SEF that the Commission may adopt. For example, a SB SEF could operate both a multi-dealer RFQ mechanism for the trading of less liquid SB swaps and a limit order book for the trading of more liquid SB swaps.

The Commission has considered whether brokerage trading, as described above, would satisfy its proposed interpretation of the definition of SB SEF. On the one hand, brokerage trading relies to a certain degree on "voice" communication, such as telephonic communication between the broker and its customers. On the other hand, the wholesale broker[46] acts as an intermediary between various potential participants to a SB swap transaction, and may utilize electronic systems to display trading interest with which various participants could interact to transact in SB swaps. In some respects, the wholesale broker's role is similar to that of a floor broker on an exchange, in which the floor broker may use voice communication to find trading interest on the floor that can interact with an order from its customer. If after the wholesale broker receives a request from a customer (of which there must be more than one, but which do not need to be acting simultaneously) to execute a trade in a SB swap, and the broker then submits that request to all participants on the system or platform (or to less than all participants, if the customer has chosen to have the request sent to less than all participants), the Commission preliminarily believes that such a model could satisfy the Commission's proposed interpretation of the definition of SB SEF. Thus, the brokerage trading model may be able to satisfy the Commission's proposed interpretation of the definition of SB SEF to the extent that multiple participants would have access to the system or platform and their trading interest could interact with bids and offers of multiple other participants in that system or platform. Unless explicitly requested by the customer, for any given transaction if a wholesale broker typically acts only as the intermediary between a given customer and a single counterparty to facilitate the negotiation of a bilateral contract, the Commission does not believe this wholesale broker would meet the proposed interpretation of the definition of SB SEF. Because of the different variations of the wholesale broker system, however, each system would have to be evaluated on its own merits to determine whether it would meet the Commission's proposed interpretation of the definition of SB SEF.

The Commission's proposed interpretation of the definition of SB SEF would result in permitting to be registered as SB SEFs systems or platforms for the trading of SB swaps with a variety of features, and not just those systems or platforms with exchange-like features (for example, systems requiring all trading interest to be firm and displayed to all participants in the market). The concern with taking the latter approach is that the market for many SB swaps is fairly illiquid.[47] However, in the context of SB swaps that are subject to the mandatory clearing requirement, the Exchange Act requires that the trading of SB swaps must occur on a SB SEF or on an exchange, if the SB swap is made available for trading (unless certain exceptions apply). Thus, requiring every registered SB SEF to operate like a national securities exchange could result in (1) cleared SB swaps not being made available to trade on an exchange or SB SEF, with the result that SB swaps would continue to trade in the OTC SB swap market; or (2) if SB swaps subject to mandatory clearing are made available to trade on an exchange or SB SEF, the continued development of the SB swap market could be hindered, if participants are unwilling to display two-sided firm quotes to participants or if the requirement to do so results in bid-offer spreads that are so wide as to not be economical). If the definition of SB SEF is too narrowly construed, this could provide a disincentive for SB swap trading activity to move from the OTC swap market to regulated markets. A broader interpretation of the definition of SB SEF could have the beneficial result of increasing the proportion of trading occurring on regulated markets. Conversely, if the definition of SB SEF is too broadly construed, the Commission's regulatory scheme may not adequately advance the Dodd-Frank Act's goal of greater transparency. The Commission's proposed interpretation of the definition of SB SEF is intended to balance these concerns, promoting transparency as well as providing incentives for market participants to trade SB swaps on regulated markets pursuant to Commission rules and oversight, rather than in the OTC swap market.

The Commission notes that no matter what other functionality a SB SEF puts in place (for example, a multi-dealer electronic RFQ mechanism), it also would be required to provide a basic functionality to allow any participant on the SB SEF the ability to make and display executable bids or offers accessible to all other participants on the SB SEF, if the market participant chooses to do so.

Considering the early stage of development of the regulatory framework for the SB swap market and the existing structure of the SB swap market, the Commission is mindful that its interpretation of the definition of SB SEF, and the rules it is proposing herein to implement the Dodd-Frank Act, could have unforeseen consequences, either beneficial or undesirable, with respect to the shape that this market will take. In the Commission's view, it is important that the regulatory structure will provide incentives for the trading of SB swaps on regulated markets that are designed to foster greater transparency and competition that are subject to Commission oversight, while at the same time allow for the continued efficient innovation and evolution of the SB swap market. The Commission therefore is seeking where appropriate to take a deliberate and attentive approach to the regulation of SB SEFs that is informed by the state of development of the trading of SB swaps on regulated markets.

C. Request for Comments

The Commission seeks commenters' views and suggestions on its proposed interpretation of the definition of SB SEF. Comment is requested on whether the Commission's proposed interpretation, which would require an RFQ to be sent to all participants but would allow the quote requesting participant to query less than all participants, is appropriate, or whether it is too narrow or too broad. Are there other interpretations of the statutory definition that would promote price transparency and competition, as well as incenting market participants to trade on SB SEFs rather than in the OTC market? If so, please explain. Does the proposed ability of the quote requesting participant to choose to send a RFQ to less than all participants, raise any concerns? Should the decision to

[46] For purposes of this proposing release, the term "wholesale brokers" generally refers to brokers that intermediate transactions in SB swaps between dealers or between dealers and end users.

[47] *See supra* note 35.

exercise the ability to choose to send a RFQ to less than all participants be required on a transaction-by-transaction basis? Why or why not? When should the opt-out feature be permitted other than on a transaction-by-transaction basis? What would be the potential benefits or costs of allowing an RFQ to be submitted to only one participant? What would be the potential benefits or costs of requiring that an RFQ be sent to more than one participant? If the Commission were to require that an RFQ be sent to more than one participant, how many should be the minimum? Should the Commission require that an RFQ be sent to two participants? Five participants (which is the number proposed by the CFTC)? [48] Or some other number of participants? Which approach—allowing a RFQ to be sent to one participant or requiring a minimum number greater than one—would better promote transparency? Which approach would encourage greater trading of SB swaps on SB SEFs? What impact, if any, would the various approaches have on market participants' incentives to trade within the United States or in other jurisdictions? How should the Commission weigh the possibility that trading may move to other jurisdictions in determining how best to regulate markets within the United States? What would be the costs and benefits to such an approach? What if only a small number of dealers were willing to provide quotes on the platform or in a particular SB swap?

Should the proposed interpretation that affords the ability to opt to have a RFQ sent to less than all participants be limited to block trades? Should a proposed interpretation that affords the ability to opt to have a RFQ sent to one participant be limited to block trades? What would be the benefits and costs of allowing the opt-out flexibility, to any number of participants, for block trades? For non-block trades? Are there factors that would cause a different result for block trades versus non-block trades? Would the flexibility for participants to choose to send a RFQ to less than all participants, including to just one participant, help to address concerns about the impact of pre-trade transparency on dealers' incentives or ability to provide competitive prices, as discussed more fully in Section VIII.C? If so, how so? If not, why not?

The Commission also is interested in learning commenters' views on whether the market for SB swaps would be enhanced or adversely affected by its proposed interpretation of the definition of SB SEF and, if so, in what ways.

Should there be a requirement that the execution of trades or the submission of bids and offers be done electronically?

Would the proposed requirement that an SB SEF provide functionality to allow any participant on an SB SEF to make and display executable bids or offers accessible to all market participants on the SB SEF, if the market participants choose to do so, be beneficial? What, if any, impact would requiring this functionality have on access to the SB SEF, or liquidity of the SB swaps traded on the SB SEF? Should the proposed requirement be modified? If so, how? What would be the advantages and disadvantages of such a proposal? Do commenters believe that market participants would utilize this functionality? Should the Commission require any particular method of displaying such bids or offers? For example, should the Commission require that the SB SEF post all of these executable bids and offers on a centralized screen visible by all participants? What would be the advantages and disadvantages of having such a centralized screen? What other method could be utilized to display such bids and offers?

In addition, the Commission requests comment on the consequences of its proposed interpretation of the definition of SB SEF on existing platforms that may seek to register as a SB SEF and on those platforms that would not be able to meet the proposed interpretation of the definition of SB SEF. What kinds of changes would existing platforms need to make to their current structure to fall within the proposed interpretation of the definition of SB SEF? Are there existing platforms that would not be able to restructure to meet the proposed interpretation, *e.g.,* single-dealer RFQ platforms? If so, what impact, if any, would that outcome have on the market for SB swaps? Are single-dealer platforms likely to become obsolete as trading of certain SB swaps moves to SB SEFs? Or, are such platforms likely to continue to exist to support the OTC market? What impact would the proposed interpretation have on competition among existing trading platforms and liquidity in SB swaps as trading of certain SB swaps moves to SB SEFs? Are new platforms likely to emerge to trade SB swaps?

The Commission is interested in learning commenters' views on the effect on the SB swap market if certain trading platforms would not meet the proposed interpretation of the definition of SB SEF and would not be able to register as a SB SEF, and therefore no longer would be able to trade SB swaps that are subject to mandatory clearing and are made available to trade on a SB SEF or an exchange. Are there any types of trading venues so critical to the proper functioning of the SB swap market that the Commission should consider expanding the proposed interpretation of the definition of SB SEF so that such entities could qualify as SB SEFs? If so, what trading platforms are they and what kinds of conditions should they be subject to? Should any such expansion of the proposed interpretation of the definition of SB SEF to cover such platforms be temporary and, if so, for how long? What would be the impact of such action on any platform that could meet an unexpanded definition of SB SEF? Market participants have expressed concern about the trading of illiquid SB swaps once platforms are configured to meet the statutory definition of SB SEF, particularly in light of the mandatory trade execution requirement. The Commission requests comment on the effect of its proposed interpretation of the definition of SB SEF on the trading of illiquid SB swaps. Would a multi-dealer RFQ system as discussed above sufficiently accommodate the trading of illiquid SB swaps? If not, what other models could meet the statutory definition of SB SEF and accommodate the trading of illiquid SB swaps? Would an interpretation of the definition of SB SEF that would allow an investor to choose to send an RFQ to one participant effectively accommodate the trading of illiquid SB swaps? Would an interpretation of the definition of SB SEF that would require that an RFQ be sent to more than one participant effectively accommodate the trading of illiquid SB swaps? In responding to these questions, the Commission requests that commenters take into account the Commission's discussion of SB swaps that are made available to trade in Section VIII.B below.

The discussion above contains several examples of trading models that the Commission believes would meet the statutory definition of SB SEF. Are there other trading models not discussed above that would meet the statutory definition of SB SEF? The discussion above also contains several examples of trading models that the Commission believes would not meet the statutory definition of SB SEF. Are there other models that should be excluded from the proposed interpretation?

The Commission seeks commenters' views on the role of wholesale brokers in the SB swap market and its view that trading of SB swaps by such brokers

[48] *See* Notice of proposed SEF rulemaking by the CFTC, *supra* note 17 (requiring that RFQs be disseminated to at least five participants).

potentially could satisfy the proposed interpretation of the definition of SB SEF. As noted above, the Commission has identified bilateral negotiation, *e.g.,* a trade occurring between two parties via the telephone, as a model that would not meet its proposed interpretation of the definition of a SB SEF. The Commission understands that wholesale brokers often act as intermediaries in executing SB swap transactions and may engage in bilateral negotiation when they attempt to complete an order. The Commission further understands that the orders that wholesale brokers attempt to fill may be large and that, as a result, they may interact with multiple participants in attempting to execute the transactions. The Commission also understands that these brokers may also maintain electronic systems for the display of trading interest that their customers can access. Do commenters agree that bilateral negotiation by wholesale brokers, by itself, should not meet the proposed interpretation of the definition of SB SEF? Is the Commission's view correct that there are ways in which wholesale brokers could restructure their operations to meet the proposed interpretation of the definition of SB SEF? How would such platforms or systems be structured to meet the proposed interpretation? What would be the impact on the SB swap market of any restructuring of a wholesale broker's business to meet the Commission's proposed interpretation of the definition of SB SEF, particularly in light of the fact that trades in SB swaps today frequently occur through bilateral negotiation? For those wholesale brokers that currently effect transactions in SB swaps, would the modifications that a wholesale brokerage firm would be required to make to satisfy the proposed interpretation of the definition of SB SEF, the proposed rules implementing the Core Principles, and the proposed registration requirements be too costly or otherwise impracticable to meet so that the firm would find it difficult to register as a SB SEF? The Commission recognizes that wholesale brokerage activities differ from dealer to customer activities in effecting SB swap transactions. Certain proposed requirements discussed below, such as impartial access, may affect wholesale brokers differently than SB SEFs that are not operated by such brokers. Comment is requested on any such different impact on wholesale brokers that intend to operate SB SEFs, including the costs and benefits of such impact. Should the Commission view wholesale brokers' SB SEF operations differently than the operations of other SB SEFs? If so, how so?

Another example of a trading platform that could meet the proposed interpretation of the definition of SB SEF would include a multi-dealer RFQ model. Do commenters agree that the definition of SB SEF should cover these types of trading platforms? If so, why? If not, why not?

Market participants also have expressed concern about any proposed interpretation of the definition of SB SEF that would result in others discerning their proprietary trading strategies. What would be the impact of the Commission's proposed interpretation of the definition of SB SEF on these concerns? Would one or more of the models discussed above that would meet the proposed interpretation of the definition of SB SEF provide an adequate level of comfort for these market participants? If not, is there a model that would meet the statutory definition of a SB SEF and yet account for these market participants' concerns?

As noted above, the Commission recognizes that the regulatory framework for the SB swap market is still in its early stages of development. What would be the impact on innovation in the SB swap market as a result of the proposed interpretation of the definition of SB SEF?

For example, under the proposed interpretation of the definition of a SB SEF, the SB SEF must provide a mechanism for the dissemination of firm quotes, if any, submitted by participants in the SB SEF. This functionality would allow a "limit order-book" model to emerge in parallel with other trading models on the SB SEF, including RFQ mechanisms, provided that each model meets all SB SEF requirements discussed above. The proposed interpretation is based on the premise that allowing more than one type of trading model to qualify as a SB SEF would, among other things, provide investors with more choices as well as encourage more types of SB swaps to trade on venues regulated by the Commission. Is there any scenario where this flexibility could impact competition or innovation because dealers may have their own preferences for one model over another? If so, under what scenario could this occur, and what consequences could result? For example, would the concentration of trading in the SB swap market raise concerns that, and provide incentives for, market participants that have a significant portion of the trading volume for certain types of SB swaps in one type of market structure to resist trading those SB swaps in a market structure that might otherwise be more efficient for that particular product?

The Commission also is interested in learning whether its proposed interpretation of the definition of SB SEF would influence market participants' decisions regarding the jurisdiction in which to execute their SB swap trades. Would the proposed interpretation affect a market participant's decision as to the jurisdiction in which to execute SB swaps transactions? If so, how? What other factors might also influence that decision, and how would those factors weigh against this factor? The Commission seeks commenters' views on whether, the ways in which, and to whom any migration to a different jurisdiction would be beneficial or adverse.

Commenters are urged, when considering all questions regarding the Commission's proposed interpretation of the definition of SB SEF, to take into account the rules being proposed by the Commission to implement the Core Principles, particularly the rules regarding the treatment and interaction of trading interest on a SB SEF, as discussed below.[49] The 14 Core Principles set forth in Section 3D(d) of the Exchange Act are integral to the regulation of a SB SEF. The Commission, in Sections VIII to XXII of this release, is proposing various rules to implement these Core Principles, as well as proposed registration requirements. The Commission also is interested in commenters' views on whether the Commission's proposed interpretation of the definition of SB SEF, along with its proposed rules implementing the Core Principles and proposed registration requirements, in the aggregate, are too permissive, are appropriate, or are too burdensome at this stage of development of the SB swap market. If commenters believe that the proposals in the aggregate are too permissive, the Commission is interested in being informed of ways in which they could be enhanced. If commenters believe that the proposals in the aggregate are too burdensome, the Commission is interested in being informed of ways in which they could be modified.

The Commission is interested in learning commenters' views on whether the combination of the proposed interpretation of the definition of SB SEF, its proposed rules implementing the Core Principles, and its proposed registration requirements would be too

[49] *See infra* Section VIII (discussing Core Principle 2 and the requirements relating to a SB SEF's trading rules).

onerous and thus would make it impractical or economically infeasible for entities that currently trade SB swaps to modify their procedures, personnel, systems or platform in order to operate as a SB SEF. If this is the case, the Commission seeks commenters views on ways that its proposed interpretation of the definition of SB SEF, its proposed rules implementing the Core Principles, or its proposed registration requirements could be modified so that entities that currently trade SB swaps could continue to do so and at the same time the statutory requirements of the Dodd-Frank Act relating to SB SEFs would be met. In particular, the Commission requests comment on the question of whether it should adopt a phased approach to the implementation and/or application of the proposed rules, whereby certain provisions would become operational only when certain designated timing, volume, liquidity, or other thresholds were met.[50] The Commission seeks commenters' views on the steps it could take to facilitate the transition to a more regulatory environment for those entities that currently trade SB swaps and expect to register as SB SEFs.[51]

IV. Exemption From the Definition of Exchange for Security-Based Swap Execution Facilities

An entity that meets the definition of SB SEF in Section 3(a)(77) of the Exchange Act may also meet the definition of "exchange" set forth in Section 3(a)(1) of the Exchange Act,[52] certain of the terms of which have been interpreted by the Commission in Rule 3b–16 of the Exchange Act.[53] The Commission believes that Congress did not intend that entities that meet the definition of SB SEF in Section 3(a)(77) of the Exchange Act and that comply with Section 3D of the Exchange Act and the rules and regulations promulgated by the Commission (including the requirement to register as a SB SEF) also would be subject to various requirements applicable to exchanges, including registration as a national securities exchange.[54]

Section 3(a)(77) of the Exchange Act defines a SB SEF as a trading system or platform in which multiple participants have the ability to execute or trade SB 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: (1) Facilitates the execution of SB swaps between persons; and (2) *is not a national securities exchange* (emphasis added).[55] Further, Section 3C(h) of the Exchange Act provides that transactions involving SB swaps subject to the clearing requirement be executed on either (1) an exchange or (2) a SB SEF registered under Section 3D of the Exchange Act or exempt from registration (unless no exchange or SB SEF makes the SB swap available to trade or the SB swap transaction is subject to a clearing exception).[56] Finally, Section 3D(a)(1) of the Exchange Act provides that no person may operate a facility for the trading or processing of SB swaps, unless the facility is registered as a SB SEF or as a national securities exchange.[57] The Commission interprets these provisions to mean that an entity that is registered as a SB SEF cannot also be a national securities exchange; that an exchange and a SB SEF registered under Section 3D of the Exchange Act (or exempt from such registration) are separate categories of regulated entities for the trading of SB swaps; and that an entity registered as a SB SEF would not also be required to register as a national securities exchange.

Section 36 of the Exchange Act[58] gives the Commission broad authority to exempt any person, security, or transaction from any provision of the Exchange Act and any rule or regulation thereunder. Such an exemption may be subject to conditions. Using this authority, the Commission is proposing to amend Rule 3a1–1 of the Exchange Act[59] by adding paragraph (a)(4) to exempt any SB SEF from the definition of "exchange," if such SB SEF provides a marketplace solely for the trading of SB swaps (and no other security) and complies with the provisions of proposed Regulation SB SEF.[60] The effect of this exemption would be that an entity that registers as a SB SEF would not also have to register as a national securities exchange.

The Commission preliminarily believes that this proposed exemption is necessary and appropriate in the public interest and is consistent with the protection of investors because it would effectuate the intent of the Dodd-Frank Act, as expressed in Sections 3(a)(77), 3C(h) and 3D(a)(1) of the Exchange Act, and it would eliminate what the Commission believes would be a largely duplicative oversight of SB SEFs. The Commission believes that Congress specifically provided a comprehensive regulatory framework for SB SEFs in the Exchange Act, as amended by the Dodd-Frank Act, and therefore that such entities that are registered as SB SEFs should not also be required to register and be regulated as national securities exchanges. The Commission notes that a registered SB SEF that chose to provide a marketplace for the trading of any security other than a SB swap would not be in compliance with the exemption in proposed Rule 3a1–1(a)(4). Also, as the SB swaps markets continue to evolve, the Commission will continue to assess the appropriateness of, and/or take action with respect to, the proposed exemption from the definition of exchange.

The Commission requests comment on the proposed exemption in Rule 3a1–1(a)(4). Is the exemption necessary or appropriate? Are the conditions to the proposed exemption appropriate or should there be any additional

[50] *See infra* the discussion in Section XXV regarding a phased approach to implementation.

[51] *See infra* Section XXI.A.2 seeking commenters' views on a possible phased-in approach to any rules that the Commission may adopt with respect to SB SEFs.

[52] 15 U.S.C. 78c(a)(1). The term "exchange" means any organization, association, or group of persons, whether incorporated or unincorporated, which constitutes, maintains, or provides a market place or facilities for bringing together purchasers and sellers of securities or for otherwise performing with respect to securities the functions commonly performed by a stock exchange as that term is generally understood, and includes the market place and the market facilities maintained by such exchange.

[53] 17 CFR 240.3b–16 defines the phrase "market place or facilities for bringing together purchasers or sellers of securities or for otherwise performing with respect to securities the functions commonly performed by a stock exchange" to mean an organization, association or group of persons that (1) brings together the orders for securities of multiple buyers and sellers; and (2) uses established, non-discretionary methods (whether by providing a trading facility or by setting rules) under which such orders interact with each other, and the buyers and sellers entering such orders agree to the terms of the trade.

[54] *See, e.g.,* Section 6 of the Exchange Act, 15 U.S.C. 78f, which, among other things, requires a national securities exchange to enforce compliance by its members and their associated persons with the Exchange Act and rules and regulations thereunder, as well as with the exchange's rules. National securities exchanges are self-regulatory organizations ("SROs") for purposes of the Exchange Act and are subject to the requirements of Sections 17 and 19 of the Exchange Act, 15 U.S.C. 78q and78s. Section 17(a)(1) requires national securities exchanges to make and keep records for prescribed periods, and to furnish such records to the Commission as well as any related reports. Section 19(b) requires, among other things, SROs to file proposed rule changes with the Commission.

[55] *See* Public Law 111–203, § 761(a) (adding Section 3a(77) of the Exchange Act).

[56] *See* Public Law 111–203, § 763(a) (adding Section 3C(h) of the Exchange Act). The Commission notes that in this section Congress chose to use the term "exchange" as opposed to "national securities exchange." An exchange only becomes a "national securities exchange" upon registration with the Commission pursuant to Section 6 of the Exchange Act.

[57] *See* Public Law 111–203, § 763(c) (adding Section 3D(a)(1) of the Exchange Act).

[58] 15 U.S.C. 78mm.

[59] 17 CFR 240.3a1–1.

[60] *See* proposed Rule 3a1–1(a)(4).

conditions? What are the benefits or drawbacks of the proposed exemption?

The definition of "security-based swap execution facility" and the definition of "exchange" (certain terms of which have been interpreted by Rule 3b–16 under the Exchange Act) are similar in that they both include the concept of multiple participants and multiple buyers and sellers, respectively. However, these definitions are not identical. It is possible that an entity that trades SB swaps would meet the criteria of Rule 3b–16 but not the definition of SB SEF contained in Section 3(a)(77) of the Exchange Act. If such an entity trades SB swaps that are subject to mandatory clearing and that are made available to trade on an exchange or SB SEF, it would be required to register as a national securities exchange, absent a limited volume exemption pursuant to Section 5 of the Exchange Act.[61] Should the Commission permit such a platform to register as a SB SEF pursuant to Section 3D(a)(1) of the Exchange Act?[62] Should the Commission instead provide an exemption from the definition of exchange for such an entity? If so, why, and what should be the conditions to any such exemption? What would be the benefits or drawbacks of any such exemption?

V. Conditional Exemption From Regulation as Brokers for Security-Based Swap Execution Facilities

An entity that meets the definition of "security-based swap execution facility" in Section 3(a)(77) of the Exchange Act also would meet the definition of "broker" set forth in Section 3(a)(4) of the Exchange Act.[63] The term "broker" is generally defined to mean any person engaged in the business of effecting transactions in securities for the account of others.[64] A SB SEF is defined as a trading system or platform in which multiple participants have the ability to execute or trade SB 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 SB swaps between persons; and (B) is not a national securities exchange.[65] A SB SEF, by facilitating the execution of SB swaps between persons, also would be engaged in the business of effecting transactions in securities for the account of others and therefore would meet the statutory definition of "broker." Absent an exception or exemption, a SB SEF that effects transactions in SB swaps would be required to register as a broker pursuant to Sections 15(a)(1) and (b) of the Exchange Act[66] and to comply with the reporting and other requirements applicable to brokers under the Exchange Act and rules and regulations thereunder.

As the Commission noted in its discussion regarding the exemption from the definition of "exchange" for SB SEFs, the Exchange Act, as amended by the Dodd-Frank Act, sets forth a comprehensive regulatory framework for SB SEFs. The Commission believes that this framework indicates that Congress did not intend for entities that meet the definition of SB SEF in Section 3(a)(77) of the Exchange Act and that comply with Section 3D of the Exchange Act and the rules and regulations thereunder (including the registration as a SB SEF) also to be subject to all of the requirements set forth in the Exchange Act and the rules and regulations thereunder applicable to brokers.[67] As discussed above, the Exchange Act, as amended, establishes the statutory structure for SB SEFs to register with the Commission and for the Commission to adopt rules and regulations that require these entities to comply with the Core Principles and enforce compliance with those Core Principles and any rules or regulations that the Commission may adopt.

Section 36 of the Exchange Act gives the Commission broad authority to exempt any person, security, or transaction from provisions of the Exchange Act and the rules thereunder.[68] Such an exemption may be subject to conditions.[69] Using this authority, as well as its authority to establish procedures regarding the registration of brokers, the Commission is proposing Rule 15a–12 under the Exchange Act to allow a SB SEF that is a broker solely due to its activity with respect to SB swaps executed on or through the SB SEF to satisfy the requirement to register as a broker by registering as a SB SEF. Such person, however, must not engage in any activity that would require registration as a broker other than facilitating the trading of SB swaps on or through the SB SEF in a manner consistent with Regulation SB SEF. For example, acting as an agent to a counterparty to a SB swap trade or acting in a discretionary manner with respect to the execution of a SB swap trade would indicate that such person may be acting as a broker and, if the person is acting as a broker, it would be required to register as such, unless an exemption or exception from registration was available. If an entity, such as an inter-dealer broker, for example, elects not to separate its inter-

[61] The trading of a SB swap on an ATS when that SB swap is subject to mandatory clearing and is made available to trade on a SB SEF or a national securities exchange would not satisfy the requirement of Section 3C(h) of the Exchange Act. Section 3C(h) of the Exchange Act states that, with respect to transactions involving SB swaps subject to the clearing requirement of subsection (a)(1) of Section 3C of the Exchange Act, the counterparties shall (A) execute the transaction on an exchange; or (B) execute the transaction on a SB SEF registered under Section 3D of the Exchange Act or a SB SEF that is exempt from registration under section 3D(e) of the Exchange Act. Although, as noted above, Section 3C(h) uses the term "exchange" as opposed to "national securities exchange," an ATS would not satisfy this requirement because an ATS is exempt from the definition of exchange pursuant to Rule 3a1–1 under the Exchange Act.

[62] Section 3D(a)(1) of the Exchange Act states that "no person may operate a facility for the trading or processing of security-based swaps, unless the facility is registered as a security-based swap execution facility or as a national securities exchange under this section." Section 3(a)(77) of the Exchange Act defines "security-based swap execution facility" to mean a trading system or platform in which multiple participants have the ability to execute or trade SB 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 SB swaps between persons; and (B) is not a national securities exchange. The Commission interprets these two provisions, taken together, to require registration as a SB SEF or a national securities exchange for any entity that meets the definition of SB SEF in Section 3(a)(77) of the Exchange Act.

[63] 15 U.S.C. 78c(a)(4).

[64] *Id.* The term "security" in Section 3(a)(10) of the Exchange Act includes a "security-based swap." *See* 15 U.S.C. 78c(a)(10).

[65] *See* Public Law 111–203, § 761(a) (adding Section 3(a)(77) of the Exchange Act).

[66] 15 U.S.C. 78o(a)(1) and (b). Section 15(a)(1) generally provides that, absent an exception or exemption, a broker or dealer that uses the mails or any means of interstate commerce to effect transactions in, or to induce or attempt to induce the purchase or sale of, any security must register with the Commission. Section 15(b) generally provides the manner of registration of brokers and dealers and other requirements applicable to registered brokers and dealers.

[67] Brokers and dealers must comply with the Exchange Act provisions and rules and regulations thereunder applicable to them. *See, e.g.,* Section 15 of the Exchange Act, 15 U.S.C. 78o, and rules and regulations thereunder. For example, brokers and dealers must comply with a number of regulations that govern their conduct, such as rules relating to customer confirmations and disclosure of credit terms in margin transactions. *See* 17 CFR 240.10b–10 and 17 CFR 240.10b–16. They also must comply with a number of financial responsibility regulations, such as the net capital and customer protection rules. *See* 17 CFR 240.15c3–1 and 17 CFR 240.15c3–3. Among other things, registered brokers and dealers also must make and keep current books and records relating to their business and detailing, among other things, securities transactions, money balances, and securities positions; keep records for required periods and furnish copies of those records to the Commission on request; and file certain financial reports with the Commission. *See* 17 CFR 240.17a–3, 17 CFR 240.17a–4, and 17 CFR 240.17a–5.

[68] 15 U.S.C. 78mm.

[69] *See id.*

dealer broker from its SB SEF or create a subsidiary for its SB SEF, and instead chooses to operate the SB SEF as the same entity as the broker, the inter-dealer broker would not qualify for the exemption.

In addition, the Commission is proposing to conditionally exempt any SB SEF from the Exchange Act and the rules and regulations thereunder applicable to brokers, except Exchange Act Sections 15(b)(4), 15(b)(6), and 17(b).[70] Under the proposed Rule, three key provisions of the Exchange Act that serve as the basis for Commission examination and enforcement of the Federal securities laws with respect to a registered broker would continue to apply to a SB SEF that relies on the exemption in proposed Rule 15a–12. Section 17(b) of the Exchange Act[71] authorizes the Commission to conduct reasonable periodic, special, or other examinations, of "[a]ll records" maintained by entities described in Section 17(a),[72] including registered brokers.[73] These examinations may be conducted "at any time, or from time to time," as the Commission "deems necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of [the Exchange Act]."[74] Proposed Rule 15a–12 also would not exempt a broker that registers as a SB SEF from the statutory disqualification provisions in Sections 15(b)(4) and (6) of the Exchange Act, both with respect to itself and with respect to its associated persons.[75] Further, pursuant to proposed Rule 15a–12(d), a broker registered under Section 15a–12(a) of the Exchange Act that does not engage in any activity other than the facilitating and trading of SB swaps on or through the SB SEF in a manner consistent with Regulation SB SEF would be exempt from the Securities Investor Protection Act ("SIPA"), including membership in the Securities Investor Protection Corporation.[76]

The Commission believes that the exemption in proposed Rule 15a–12 under the Exchange Act is necessary and appropriate in the public interest and consistent with the protection of investors because it would eliminate what the Commission believes would be unnecessary additional regulation of SB SEFs. Because SB SEFs would be required to register as such under Section 3D of the Exchange Act, it would be unnecessary for them also to be subject to statutory and regulatory provisions governing brokers, subject to certain exceptions set forth in the proposed rule. The Commission believes that Congress specifically provided a comprehensive regulatory framework for SB SEFs in the Exchange Act, as amended by the Dodd-Frank Act, and therefore that such entities generally should not also be regulated as brokers where such regulation would be duplicative and unnecessary. As such, the Commission preliminarily believes that the broker registration and oversight process can be accomplished largely through the entity's registration as a SB SEF. In this regard, the Commission also believes that it would be unnecessary and inconsistent with the comprehensive regulatory framework for SB SEFs to require a SB SEF, which would not be a custodian of customer funds or securities and would not otherwise operate as a broker, to comply with SIPA. SIPA is a comprehensive regulatory scheme for the orderly liquidation of failed broker-dealers and the return of customer property. If additional regulation is developed for brokers, any application of such regulation to SB SEFs would be proposed by rule. Any order, such as a suspension of the registration or trading of a security pursuant to Sections 12(j) or 12(k) of the Exchange Act,[77] if applicable to a SB SEF, would specify that it would be applicable to a SB SEF.

The Commission notes that it is not exempting SB SEFs from registration as brokers; rather, it is proposing to eliminate an additive layer of regulation that the Commission believes is not necessary in light of its regulatory oversight of SB SEFs. The Commission does not believe, however, that it would be in the public interest to exempt SB SEFs from the examination requirements of Section 17(b) of the Exchange Act, the statutory disqualification provisions of Sections 15(b)(4) and (6) of the Exchange Act.

The Commission requests comment on all aspects of its proposed rule. Specifically, the Commission requests comment on the scope, form, and conditions of the proposed exemption. Is the exemption necessary? Should the Commission add additional conditions to its exemption, including requiring compliance with any other statutory provisions or any other rules or regulations applicable to brokers? If so, which ones, and why? Should the Commission exempt SB SEFs from the provisions of SIPA? If not, why not?

The Commission seeks comment on whether there is a need for SB SEFs to become members of a national securities association. Would it be beneficial to require SB SEFs to become members of a national securities association to provide an additional level of regulatory oversight in addition to oversight by the Commission? Why or why not? Should the proposed exemption include a condition requiring SB SEFs to comply with Section 15(b)(8) under the Exchange Act,[78] which requires a registered broker to be a member of a registered national securities association unless such broker effects transactions solely on a national securities exchange of which it is a member? What would be the advantages or disadvantages of such membership?

As noted above, the proposed Rule would not apply in those instances when the SB SEF is engaging in activity that is not solely related to the execution of SB swaps on or through the facility, *e.g.,* when the broker provides services such as acting as an agent to a counterparty to an SB swap trade or acts in a discretionary manner with respect to the execution of SB swap trades. In such instances, should the broker be required to comply with all Exchange Act and Commission requirements relating to brokers? If so, how would the broker be able to separate its brokerage function from its activities as a SB SEF? What potential conflict concerns would be raised, if any, if an entity that was engaged in brokerage activity in SB swaps on a SB SEF were affiliated with that SB SEF, or if an entity were engaging in brokerage activity in SB swaps on a SB SEF in the same legal entity that operates the SB SEF? If commenters believe that such activity would raise concerns, should the Commission require the entity's brokerage activities and its SB SEF activities to be conducted on separate legal entities? Or, should the Commission impose requirements on the ability of a broker to be affiliated with a SB SEF? If so, what conditions should the Commission impose, and how would they address any potential conflict concerns?

Are there any potential conflict concerns raised if a wholesale broker is affiliated with a SB SEF, or is operating

[70] *See* proposed Rule 15a–12(c).

[71] 15 U.S.C. 78q(b). *See also* 15 U.S.C. 78m(h)(4).

[72] 15 U.S.C. 78q(a).

[73] 15 U.S.C. 78q(b).

[74] *Id.*

[75] 15 U.S.C. 78o(b)(4) and (6). *See also* 15 U.S.C. 78c(a)(18) (defining "person associated with a broker or dealer" or "associated person of a broker or dealer").

[76] Section 36 of the Exchange Act gives the Commission broad authority to exempt any person, security, or transaction from any of the provisions of the Exchange Act. This authority would include the ability of the Commission to grant an exemption under Section 36 from certain requirements of SIPA. *See* Securities Exchange Act Release No. 40594 (October 23, 1998), 63 FR 59362, 59366, n. 31 (November 3, 1998).

[77] 15 U.S.C. 78*l*(j) and (k).

[78] 15 U.S.C. 78o(b)(8).

in the same legal entity as a SB SEF? If so, what are those concerns, and what are commenters views on whether and how such concerns should be addressed?

What would be the effect of having SB SEFs join a registered securities association without having a comparable SRO for security-based swap dealers ("SB swap dealers") or major security-based swap participants ("major SB swap participants")? Because SB SEFs would be subject to regulatory obligations, should the Commission provide guidance on the acceptable scope of any outsourcing of regulatory matters that the SB SEF could undertake?

VI. Access to Security-Based Swap Execution Facilities

The Dodd-Frank Act does not define the categories of market participants that may have access to trading on a registered SB SEF or the terms of such access. For the purposes of providing guidance on this issue and to ensure that SB SEFs grant access to their markets in a manner that is consistent with the Core Principles in Section 3D of the Exchange Act, the Commission is proposing Rule 809 and 811(b). Proposed Rule 809 would set forth the categories of persons that would be permitted to have direct access to trading on a registered SB SEF as a participant and also the terms and conditions that the SB SEF would need to adopt for granting such access.[79] Proposed Rule 811(b) would elaborate on the standards for providing impartial access.[80] The purpose of the proposed rules is to ensure that access to SB SEFs is granted in a manner that strikes an appropriate balance between the statutory requirements of impartial access (Core Principle 2) and financial integrity of transactions (Core Principle 6) for SB SEFs.

The Commission understands that, currently, trades in SB swaps occur among dealers on OTC inter-dealer markets, and between dealers and end-user customers on single- or multi-dealer OTC dealer-to-customer markets or through bilateral negotiations. In addition, trading of SB swaps in these OTC markets is dominated by a small number of large swap dealers.[81] When a small group of market participants dominates much of the trading in SB swaps, and exerts control over access to the SB swaps market, it raises concerns about open access and competition. If SB SEFs are controlled by a small group of dealers who also dominate trading in the market for SB swaps, the dealers may have economic incentives to exert undue influence to restrict the level of access to SB SEFs and thus impede competition by other market participants in order to increase their ability to maintain higher profit margins.[82] At the same time, in the absence of clearing or other financial safeguards, counterparties assess the degree of credit risk posed by each other, and enter into SB swap transactions only with other persons deemed to have an acceptable level of credit risk. Therefore, in the OTC market for SB swaps, open access and containing counterparty credit risk may be viewed as competing and potentially conflicting goals.

The Dodd-Frank Act addresses these competing concerns in several ways. Section 3C(a)(1) of the Exchange Act requires the mandatory clearing of SB swaps that the Commission determines must be cleared.[83] With respect to trading on SB SEFs, the Dodd-Frank Act requires SB SEFs to establish rules for both impartial access to their markets and the financial integrity of transactions on their markets, including with respect to clearance and settlement. Specifically, Core Principle 2 requires SB SEFs to provide market participants with impartial access to the market.[84] Under Core Principle 6, SB SEFs are required to establish and enforce rules and procedures for ensuring the financial integrity of SB swaps entered on or through the facilities of the SB SEF, including the clearance and settlement of SB swaps pursuant to Section 3C(a)(1) of the Exchange Act.[85] The Commission does not believe that the requirement for impartial access to a SB SEF under Core Principle 2 means that it must allow unfettered access to any and all persons. Rather, the requirements of Core Principle 6 that SB SEFs ensure the financial integrity of transactions on their markets, particularly with respect to the mandatory clearing requirement, permit SB SEF to have minimum standards for access to their markets, though such access must be provided on an impartial basis.

In recognition of the challenges in striking the balance between impartial access and financial integrity goals of the Dodd-Frank Act, and in view of the current dominance of trading in SB swaps in the OTC market by a small number of dealers, the Commission is proposing Rule 809 and Rule 811(b) to establish certain baseline principles for granting access to SB SEFs in compliance with the requirements of both Core Principles 2 and 6. Specifically, proposed Rule 809(a) through (c) and proposed Rule 811(b) would require that SB SEFs enact and apply objective standards for access to their markets, in compliance with the impartial access requirement of Core Principle 2. Proposed Rule 809(a) and (c)(1) through (4) would establish certain minimum, objective standards for SB SEF participants, in compliance with the financial integrity of transactions requirements of Core Principle 6.

A. Impartial Access

Proposed Rule 809(a) would provide that only registered SB swap dealers, major SB swap participants, or brokers (as defined in section 3(a)(4) of the Exchange Act), or eligible contract participants[86] would be eligible to

[79] *See* proposed Rule 809.

[80] *See* proposed Rule 811(b).

[81] *See* Office of the Comptroller of the Currency ("OCC"), Quarterly Report on Bank Trading and Derivatives Activities, First Quarter 2010 ("Derivatives activity in the U.S. banking system continues to be dominated by a small group of large financial institutions. Five large commercial banks represent 97% of the total banking industry notional amounts * * *."). Several commenters on proposed Regulation MC, however, took issue with this statistic because the OCC data included information about U.S. dealers only. *See, e.g.,* Letter from Barry L. Zubrow, Executive Vice President & Chief Risk Officer, JP Morgan Chase & Co., to Elizabeth M. Murphy, Secretary, Commission, and David A. Stawick, Secretary, CFTC, dated November 17, 2010.

[82] In addition, these market participants might be motivated to restrict the scope of SB swaps that are made available for trading at SB SEFs if there is a strong economic incentive to keep such SB swaps in the OTC market. Conflicts of interest concerns relating to SB SEFs are discussed in greater depth in the release proposing Regulation MC, which recently was published by the Commission as part of a rulemaking mandated by Section 765 of the Dodd-Frank Act. *See* Securities Exchange Act Release No. 63107 (October 14, 2010), 75 FR 65882 (October 26, 2010) ("Regulation MC Proposing Release"). Section 765 of the Dodd-Frank Act requires the Commission to adopt rules to mitigate specified conflicts of interest relating to SB SEFs, security-based swap clearing agencies, and SBS exchanges.

[83] *See* Public Law 111–203, § 763(a) (adding Section 3C(a)(1) of the Exchange Act). Section 3C(a)(1) makes it unlawful for a person to engage in a SB swap unless the SB swap is submitted for clearing to a registered clearing agency, if the SB swap is required to be cleared.

[84] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(2) of the Exchange Act).

[85] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(6) of the Exchange Act). Section 3C(a)(1) makes it unlawful for a person to engage in a SB swap unless the SB swap is submitted for clearing to a registered clearing agency, if the SB swap is required to be cleared. *See* Public Law 111–203, § 763(a) (adding Section 3C(a)(1) of the Exchange Act).

[86] The term "eligible contract participant" is defined in Section 3(a)(65) of the Exchange Act as having the same meaning as in Section 1a of the CEA (7 U.S.C. 1a). As discussed above, this term

Continued

become participants in a SB SEF. Proposed Rule 809(b) would require a SB SEF to permit all eligible persons that meet the requirements for becoming a participant under Rule 809(a) and the SB SEF's rules to become participants in the SB SEF, consistent with the requirements for impartial access in Core Principle 2 and proposed Rule 811(b).[87] Proposed Rule 809(b) would, however, permit a SB SEF to choose to not permit any eligible contract participants that are not registered with the Commission as a SB swap dealer, major SB swap participant, or broker (as defined in section 3(a)(4) of the Act[88]) ("non-registered ECP"), to become participants in the SB SEF. Thus, under the proposed rule, while a SB SEF could choose to not allow any non-registered ECPs to become participants, if the SB SEF chose to permit such non-registered ECPs to become participants in the SB SEF, it could not selectively prohibit certain non-registered ECPs from becoming participants if they otherwise satisfied the SB SEF's requirements. In effect, proposed Rule 809(b) would limit the discretion involved in admitting participants to a SB SEF because it would impose an affirmative requirement on SB SEFs to grant qualified persons access to their markets as participants.[89]

Proposed Rule 809(c) would require a SB SEF to establish rules setting forth requirements for eligible persons to become participants in the SB SEF consistent with the SB SEF's obligations under the Exchange Act and the rules thereunder, and includes certain enumerated minimum standards.[90] Proposed Rule 809(c), by requiring a SB SEF to codify its standards for becoming a participant in its market, would make the process of admitting participants transparent and rules-based, and thereby more objective. In addition, such rules would have to be consistent with proposed Rule 811(b), which would require every SB SEF to establish fair, objective, and not unreasonably discriminatory standards for granting impartial access to trading on the facility.[91] Proposed Rule 811(b) would require that a SB SEF may not unreasonably prohibit or limit any person with respect to access to the services offered by the SB SEF by applying those standards in an unfair or unreasonably discriminatory manner.[92] Proposed Rule 811(b)(3) also would require every SB SEF to make and keep records of all grants, denials, or limitations of access and to report that information on proposed Form SB SEF[93] and in the annual compliance report of the Chief Compliance Officer ("CCO") pursuant to proposed Rule 823(c).

As was the case when the Commission adopted Regulation ATS,[94] these provisions are based on the principle that qualified market participants should have fair access to the nation's securities markets. Under the proposal, a SB SEF would have flexibility in establishing standards for impartial access so long as those standards are fair and objective and do not unreasonably discriminate, and the SB SEF does not apply the standards in an unfair or unreasonably discriminatory manner. For example, a SB SEF could establish objective minimum capital or credit requirements for participants, as long as they were not designed to, and did not have the effect of, unreasonably discriminating among persons seeking access to the SB SEF.[95] Similarly, a SB SEF could reasonably deny access to participants based on an unfavorable disciplinary history. Provided that these or other standards are objective and applied consistently to all potential participants, a SB SEF could be considered to be granting or denying access fairly. A denial of access might be unreasonable, however, if it were based solely, for example, on the business activities of a prospective participant that are unrelated to trading on the SB SEF.[96]

The Commission believes that impartial access to SB SEFs would work in conjunction with rules proposed by the Commission to mitigate conflicts of interest that could arise when a small number of market participants, including their related persons, exercise control or undue influence over a SB SEF either through ownership of voting interests or participation in the governance of the SB SEF.[97] The Commission requests comment, however, on the extent to which both types of rules are necessary to ensure fair access to SB SEFs.

B. Financial Integrity

As noted above, proposed Rule 809(a) would permit only persons that are registered with the Commission as SB swap dealers, major SB swap participants, or brokers, or persons that are eligible contract participants (as defined in section 3(a)(65) of the Act) to become participants of a SB SEF.[98] Permitting registered SB swap dealers, major SB swap participants, and brokers to become participants would support the SB SEF's duty to ensure the financial integrity of transactions, including the clearance and settlement of SB swaps, under Core Principle 6.[99] Registered SB swap dealers, major SB swap participants, and brokers are all subject to, or would be subject to, minimum financial responsibility requirements (including margin and net capital requirements) and business conduct requirements as a result of their registered status under the Exchange Act, which the Commission believes would serve as a useful baseline for ensuring the financial integrity of their transactions entered on SB SEFs.[100]

may be further defined by the Commission and the CFTC pursuant to various sections of the Dodd-Frank Act. *See supra* note 3.

[87] Core Principle 2 requires a SB SEF to establish and enforce compliance with rules relating to any limitation on access to the facility and to provide market participants with impartial access to the market. *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(2) of the Exchange Act).

[88] 15 U.S.C. 78c(a)(4).

[89] This proposed requirement is analogous to the fair access requirement for national securities exchanges under Section 6(b)(2) of the Exchange Act, which also imposes an affirmative duty to admit qualified broker-dealers as members. *See* 15 U.S.C. 78f(b)(2). "The rules of the exchange [must] provide that any registered broker or dealer or natural person associated with a registered broker or dealer may become a member of such exchange * * *."

[90] *See* proposed Rule 809(c)(1)–(4) and *infra* notes 105–109 and accompanying text for a discussion of those proposed provisions.

[91] *See* proposed Rule 811(b)(1).

[92] *See* proposed Rule 811(b)(2).

[93] The Commission is proposing that SB SEFs register on Form SB SEF. *See infra* Section XXII for a discussion of proposed Form SB SEF.

[94] 17 CFR 242.300 *et seq. See* Securities Exchange Act Release No. 40760, (December 8, 1998), 63 FR 70844 ("ATS Adopting Release") at notes 245 to 256.

[95] *See infra* Section XII for a discussion of the ability of a SB SEF to impose higher capital requirements.

[96] The Commission also discussed fair access at length in the ATS Adopting Release. *See supra* note 94 at note 245.

[97] *See* Regulation MC Proposing Release, *supra* note 82.

[98] *See* proposed Rule 809(a). The term "participant," when used with respect to a SB SEF, would mean a person that is permitted to directly effect transactions on the SB SEF. *See* proposed Rule 800.

[99] Core Principle 6 requires SB SEFs to establish and enforce rules and procedures for ensuring the financial integrity of SB swaps entered on or through the facilities of the SB SEF, including the clearance and settlement of SB swaps pursuant to Section 3C(a)(1) of the Exchange Act. *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(6) of the Exchange Act).

[100] The Exchange Act requires registered SB swap dealers and major SB swap participants to comply with certain minimum financial responsibility and business conduct requirements. *See* Public Law 111–203, § 764(a) (adding Sections 15F(e) and (h) of the Exchange Act). The financial responsibility and business conduct requirements applicable to registered SB swap dealers and major SB swap participants will be the subject of a separate rulemaking. Likewise, the Exchange Act requires registered brokers to comply with certain financial responsibility and business conduct obligations under Section 15(c) of the Exchange Act and the rules and regulations thereunder. *See* 15 U.S.C.

Moreover, the Commission notes that these registered persons are subject to Commission oversight for compliance with those requirements.[101]

At the same time, proposed Rule 809(a) also would permit a SB SEF to choose to allow non-registered ECPs to become participants in the SB SEF. If a SB SEF chooses to permit non-registered ECPs to become participants, the SB SEF would be responsible for establishing risk management controls and supervisory procedures reasonably designed to manage financial, regulatory, and other risks associated with the eligible contract participants' access under proposed Rule 809(d).

Proposed Rule 809(d) would require SB SEFs that provide direct access to non-registered ECPs as participants to establish, document, and maintain a system of risk management controls and supervisory procedures reasonably designed to manage the financial, regulatory, and other risks of direct access by eligible contract participants.[102] The SB SEF'S risk management controls and supervisory procedures for granting access to non-registered ECPs would be required to be reasonably designed to ensure compliance with all regulatory requirements. The proposed requirements for SB SEFs in proposed Rule 809(d) are based on similar requirements in Rule 15c3–5(b) and (c)(2) under the Exchange Act for ATSs that provide access to their markets to non-broker-dealers.[103]

Allowing eligible contract participants to be direct participants in a SB SEF would be consistent with the way the OTC SB swaps market operates today. The Commission preliminarily believes that it is reasonable and appropriate to require the SB SEF that provides direct access to non-registered ECPs to undertake certain responsibilities to manage the risk of those market participants accessing their market. This proposed requirement would support the SB SEF's compliance with the financial integrity of transaction requirement of Core Principle 6. Participants that are SB swap dealers, major SB swap participants, and brokers that are participants of the SB SEFs would be required to be registered with the Commission and be subject to certain margin, net capital, and other financial requirements that, by virtue of their registration, are designed to curtail the market risk imposed by their trading activities. In contrast, non-registered ECPs would not have corresponding requirements under the Exchange Act. The proposed requirements of Rule 809(d) are designed to reduce the risks associated with non-registered ECPs that have direct access to SB SEFs by requiring SB SEFs that choose to allow non-registered ECPs to be participants to establish, document and maintain risk management controls and supervisory procedures. Since non-registered ECPs are not subject to capital and other financial requirements, there is a concern that, in the absence of requiring risk management controls and supervisory procedures, they could enter into trades that exceed appropriate credit or capital limits for their risk capacity. The Commission preliminarily believes that the SB SEF is best positioned to implement the proposed controls and procedures.

The Commission preliminarily believes that proposed Rules 809(a) and (d) would ensure that access to SB SEFs is sufficiently broad, while at the same time imposing certain thresholds and conditions for such access to ensure the financial integrity of transactions on the SB SEF. The Commission preliminarily believes that the proposed limit on eligible persons that may become participants in SB SEFs under proposed Rule 809(a) should not have the effect of preventing interested market participants from trading SB swaps. The Commission notes, for example, that many dealers would likely meet the definition of SB swap dealer, and thereby would be able to have direct access to trading SB swaps on SB SEFs once they are registered. Many other market participants would qualify for direct access by meeting the definition of "eligible contract participant" in Section 3(a)(65) of the Act. The Commission notes that, although SB SEFs are not required to provide access to their markets to non-registered ECPs as participants, if a SB SEF should provide access to non-registered ECPs to its markets as participants, it would be required to provide such access impartially consistent with proposed Rule 811(b). In addition, the Commission notes that eligible contract participants that are not participants could access a SB SEF indirectly through a participant.[104] Therefore, the Commission preliminarily believes that proposed Rule 809(a) would not have an adverse effect on access to trading SB swaps on a SB SEF.

To help ensure that access to SB SEFs is granted in a manner that would enable the SB SEF to carry out its responsibilities under Core Principle 6, proposed Rule 809(c)(1) and (2) also would require SB SEFs to have rules to require a participant to, at a minimum: (1) Be a member of, or have an arrangement with a member of, a registered clearing agency to clear trades in SB swaps that are subject to mandatory clearing pursuant to Section 3C(a)(1) of the Act and entered into by the participant on the SB SEF; and (2)(i) to meet the minimum financial responsibility requirements[105] and recordkeeping and reporting requirements[106] imposed by the Commission by virtue of its registration as a SB swap dealer, major SB swap participant, or broker, or (ii) in the case of an eligible contract participant, meet the recordkeeping and reporting requirements that the SB SEF shall establish pursuant to proposed Rule 813.

Requiring SB SEFs to put in place rules that require its participants to be a clearing member of, or have arrangements with a clearing member of, a registered clearing agency to clear trades in SB swaps that are subject to mandatory clearing and entered by the participant and, in the case of registered

78o(c), and Rules 15c1–2, 15c1–3, 15c2–1, 15c2–5, and 15c3–1 under the Exchange Act, 17 CFR 240.15c1–2, 15c1–3, 15c2–1, 15c2–5, and 15c3–1.

[101] The Commission's regulatory and oversight authority includes and would include requirements to keep books and records open to the inspection and examination authority of the Commission. *See* Section 15F(f) of the Exchange Act, Public Law 111–203, § 764 (adding Section 15F(f) of the Exchange Act) and Section 17(b) of the Exchange Act, 15 U.S.C. 78q(b).

[102] *See* proposed Rule 809(d)(1).

[103] *See* 17 CFR 240.15c3–5(c).

[104] Under the Dodd-Frank Act, transactions in SB swaps with a market participant that is not an eligible contract participant must be effected on a national securities exchange registered under Section 6(b) of the Exchange Act. *See* Public Law 111–203, § 763(e) (adding Section 6(l) of the Exchange Act). In addition, the offer and sale of SB swaps to market participants that are not eligible contract participants would have to be pursuant to an effective registration statement under Section 6 of the Securities Act of 1933. *See* 15 U.S.C. 77f.

[105] *See* Public Law 111–203, § 764(a) (adding Sections 15F(e) of the Exchange Act) and Section 15(c) of the Exchange Act, 15 U.S.C. 78o(c). For registered brokers, *see also* Rule 15c3–1 under the Exchange Act. The financial responsibility requirements applicable to registered SB swap dealers and major SB swap participants will be the subject of a separate rulemaking.

[106] The Exchange Act requires registered SB swap dealers and major SB swap participants to keep books and records of activities related to their business and provide certain reports of those activities. *See* Public Law 111–203, § 764(a) (adding Section 15F(f) of the Exchange Act). The rules relating to the recordkeeping and reporting requirements of these entities will be the subject of a separate Commission rulemaking. Likewise, the Exchange Act and rules and regulations thereunder require registered brokers to keep books and records of activities related to their business and provide certain reports of those activities. *See* Section 17(a) of the Exchange Act, 15 U.S.C. 78q(a), and *see, e.g.,* Rules 17a–3 through 17a–5 under the Exchange Act, 17 CFR 240.17a–3 through 240.17a–5.

SB swap dealers, major SB swap participants, or brokers, to meet the minimum financial responsibility requirements imposed by the Commission should strengthen the financial integrity of SB swap transactions that occur on the SB SEFs by reducing the counterparty credit risks associated with SB swap transactions, consistent with Core Principle 6.[107] Furthermore, the requirement for participants to meet the minimum recordkeeping and reporting requirements imposed by the Commission by virtue of their registration or, in the case of non-registered ECPs, those requirements imposed by the SB SEF, would enable a SB SEF to obtain the necessary information to perform their functions under Section 3D of the Exchange Act, consistent with Core Principle 5, and to enforce its rules and procedures for ensuring the financial integrity of SB swaps entered on the SB SEF, consistent with Core Principle 6.[108] The recordkeeping and reporting requirements also should foster a SB SEF's ability to comply with its obligations to capture information that may be used in establishing whether rule violations have occurred under Core Principle 2 and to monitor trading in SB swaps under Core Principle 4.[109]

Proposed Rules 809(c)(3) and (4) would require SB SEFs to have rules to require a participant to, at a minimum: (1) Agree to comply with the rules, policies, and procedures of the SB SEF, and (2) consent to disciplinary procedures of the SB SEF for violations of its rules. The Commission notes that the cooperation of participants is critical to the SB SEF's ability to comply with several Core Principles in Section 3D of the Exchange Act, particularly Core Principles 2 (Compliance with Rules), 4 (Monitoring of Trading and Trade Processing), and 6 (Financial Integrity of Transactions). For this reason, the Commission believes that it is important for SB SEFs to have rules conditioning access to their markets on a participant's compliance with the SB SEF's rules and its consent to the disciplinary procedures of the SB SEF.

The Commission requests comments on all aspects of the proposed rules relating to access on SB SEFs. The Commission also requests comments on whether proposed Rule 809 incorporates the appropriate categories of persons to be allowed direct access to SB SEFs. If not, how should the categories of such persons be altered? Should certain proposed participants be excluded from having direct access to a SB SEF? If so, which ones and why? Should other categories of persons also be allowed to have direct access to a SB SEF? If so, which ones, and why? Are there any concerns with allowing non-regulated entities to directly access a SB SEF? What would be the benefits of allowing such access? The Commission understands that it is the current practice for customers to engage in transactions with dealers without intermediation. How would the requirements of proposed Rule 809 affect that practice? Please describe any such effects. What would be the result of the proposed rule?

What are the benefits and drawbacks of the proposal for SB SEFs to provide direct access to all persons that meet the requirements for becoming a participant in their rules? Are there other alternatives that the Commission should consider to achieve the goal of having impartial access to SB SEFs, consistent with Core Principle 2? If so, please explain.

Proposed Rule 809(b) would allow a SB SEF to choose not to permit non-registered ECPs to become participants. How, if at all, would this proposed provision affect access to SB SEFs? Should the Commission allow SB SEFs to have the discretion to choose whether or not to permit non-registered ECPs to become participants? Or should the Commission mandate whether or not to require SB SEFs to allow non-registered ECPs to become participants? If the latter, should the Commission require SB SEFs to allow, or prohibit, non-registered ECPs from becoming participants? What would be the effect on access of a mandate for either option? Are SB SEFs that are capable of establishing the risk management controls and supervisory procedures required in proposed Rule 809(d) likely to exclude non-registered ECPs from becoming participants to reduce competition on their markets? Would having the flexibility to exclude non-registered ECPs from becoming participants advance the market entry of smaller SB SEFs that do not have the resources to comply with proposed Rule 809(d),[110] thus increasing opportunities for competition across SB SEFs?

Are the proposed minimum standards for participants of a SB SEF, as set forth in proposed Rule 809(c), necessary and appropriate? If not, why not? Do the qualifications for being a participant in proposed Rule 809(c)(1) and (2) adequately address the financial integrity requirements of Core Principle 6? Do the requirements of proposed Rule 809(c)(2) also foster the ability of SB SEFs to comply with their obligations under Core Principles 2, 4, and 5? What other qualifications should participants in a SB SEF be required to meet as a threshold matter? Are there other minimum standards that the Commission should consider requiring?

Are the requirements in proposed Rule 809(d) pertaining to risk management controls and supervisory procedures for SB SEFs that provide direct access to non-registered ECPs necessary or appropriate? If so, why? If not, why not and what would be a better alternative for addressing risks, if any, associated with providing access to non-registered ECPs?

The Commission recently adopted new Rule 15c3–5 to require broker-dealers to have certain risk management controls for direct and indirect access to trading on national securities exchanges and ATSs.[111] Specifically, Rule 15c3–5 imposes requirements on broker-dealers that have direct access to trading on national securities exchanges and ATSs and to broker-dealer operators of ATSs that provide direct access to non-broker-dealers. Proposed Rule 809(d) would incorporate a requirement to establish, document, and maintain a system of risk management controls and supervisory procedures reasonably designed to manage the financial, regulatory, and other risks of their business activity that is generally based upon the requirements of Rule 15c3–5(b) and (c)(2) as they apply to ATSs. However, proposed Rule 809 would not prescribe the specific components for the required risk management controls and supervisory procedures that are contained in Rule 15c3–5(c) or the other requirements in Rule 15c3–5(d) and (e). Should proposed Rule 809(d) provide more specific requirements as to the risk management controls and supervisory procedures that should apply to SB SEFs that provide access to non-registered ECPs as participants? If so, would some or all of the requirements of Rule 15c3–5(c) be appropriate for SB

[107] *See supra* note 99.

[108] *See* Public Law 111–203, § 763(c) (adding Sections 3D(d)(5) and (6) of the Exchange Act).

[109] *See* Public Law 111–203, § 763(c) (adding Sections 3D(d)(2)(B)(ii) and 3D(d)(4)(B).

[110] Proposed Rule 809(d) would require a SB SEF that choose to permit non-registered ECPs to have access as participants to establish, document, and maintain a system of risk management controls and supervisory procedures reasonably designed to manage the financial, regulatory, and other risks of this business activity and to ensure compliance with all regulatory requirements.

[111] *See* Securities Exchange Act Release No. 63241 (November 3, 2010), 75 FR 69792 (November 15, 2011) (File No. S7–03–10) (adopting release for Rule 15c3–5, which governs the terms for sponsored access or direct access on national securities exchanges and alternative trading systems).

SEFs?[112] Please specify and explain why. If not, why not and what would be a better alternative for SB SEFs in this context? Would the remaining requirements of Rule 15c3–5, in paragraphs (d) and (e), be appropriate to apply to SB SEFs that provide access to non-registered ECPs as participants?[113] At this time, the Commission is not proposing to adopt rules relating to direct or indirect access to SB SEFs for SB swap dealers, major SB swap participants, or brokers.[114] Should the Commission adopt rules for risk management controls and supervisory procedures for SB swap dealers, major SB swap participants, brokers and any other participant with direct access to trading or that may provide indirect access to trading, on a SB SEF as a participant? If so, would the terms of Rule 15c3–5 be an appropriate guideline for such rules? Please explain why or why not. If so, should the Commission apply some or all of the requirements of Rule 15c3–5 to SB swap dealers, major SB swap participants, and brokers that are participants in a SB SEF? If only some of the requirements of Rule 15c3–5 should apply, which ones should apply and why? Should the Commission apply requirements similar to those in Rule 15c3–5 only when SB swap dealers, major SB swap participants, and brokers that are participants in a SB SEF provide indirect access to the SB SEF to non-participants? Or, should the risk management controls and procedures required in Rule 15c3–5 also apply to their own transactions as participants of a SB SEF (as they do for the broker-dealers with direct access under Rule 15c3–5)? Why or why not? Or, are the terms of Rule 15c3–5 inappropriate for SB swap dealers, major SB swap participants, brokers, or other persons that are participants of a SB SEF? If so, why and what terms would be a better alternative to address the risks associated with direct access or sponsored access to SB SEFs? What other terms and conditions should the Commission consider to mitigate the risks associated with access to SB SEFs?

What would be the likely impact of having a rule like Rule 15c3–5 apply to SB swap dealers, major SB swap participants, and brokers that are participants in SB SEFs? How would current practices for trading SB swaps be affected by applying a rule like Rule 15c3–5 to participants in SB SEFs? How might the evolution of the SB swaps market over time be affected by such a rule? Would it promote or impede the establishment of SB SEFs?

VII. Core Principle 1—Compliance With Core Principles

Section 3D(d)(1) of the Exchange Act (Core Principle 1) requires a SB SEF, to be registered and maintain registration as a SB SEF with the Commission, to comply with: (i) the Core Principles described in Section 3D(d) of the Exchange Act; and (ii) any requirement that the Commission may impose by rule or regulation.[115] The Commission proposes to implement the requirements of Section 3D(d)(1) of the Exchange Act in proposed Rule 810(a) of Regulation SB SEF.

The Commission proposes in Rule 810(b) to require a SB SEF to have rules for the maintenance of certain standards of fairness in dealings with participants on their markets. The proposed requirements in Rule 810(b) are derived from similar requirements that national securities exchanges are subject to under Section 6(b) of the Exchange Act.[116] The Commission preliminarily believes that the analogous requirements incorporated into proposed Rule 810(b) are appropriate because SB SEFs, like national securities exchanges, are subject to statutory requirements to establish and enforce trading and participation rules that will deter abuses and provide impartial access to their markets.[117]

Proposed Rule 810(b)(1) would require a SB SEF to establish rules that provide for the equitable allocation of reasonable dues, fees, and other charges among its participants and any other users of its system.[118] This requirement is comparable to a similar requirement for national securities exchanges in Section 6(b)(4) of the Exchange Act.[119] SB SEFs, like exchanges, presumably would assess dues, fees, or other charges on the various market participants that trade on their markets. The purpose of this proposed requirement is to ensure that SB SEFs apply those dues, fees and other charges among participants and any other users of their systems in ways that are fair and equitable, and not in ways that inequitably favor, or discriminate against, one or more classes of such persons. Thus, proposed Rule 810(b)(1) would support the requirement in Core Principle 2 and the proposed rules thereunder that SB SEFs must provide for impartial access to their markets by ensuring that each market participant's access to the SB SEF is not limited by an inequitable distribution of dues, fees, or other charges assessed by the SB SEF.[120] In this regard, proposed Rule 810(b)(1) also is designed to promote fair competition on SB SEFs.

Proposed Rule 810(b)(2) would require a SB SEF to establish rules and systems that are not designed to permit unfair discrimination among participants and any other persons using its system. This proposed requirement is comparable to one of the requirements for national securities exchanges contained in Section 6(b)(5) of the Exchange Act.[121] In practical terms, the proposal would compel SB SEFs to design their rules and systems in ways that would treat the various market participants in the SB SEF similarly, unless appropriate considerations, consistent with the goals of the Exchange Act, provide a justification for treating some market participants differently. Like proposed

[112] Rule 15c3–5(c) requires the financial risk management controls and supervisory procedures to be reasonably designed to: (i) Prevent the entry of orders that exceed appropriate pre-set credit or capital thresholds and, where appropriate, more finely-tuned by sector, security, or otherwise by rejecting orders if such orders would exceed the applicable credit or capital thresholds; and (ii) prevent the entry of erroneous orders, by rejecting orders that exceed appropriate price or size parameters, on an order-by-order basis or over a short period of time, or that indicate duplicative orders; (iii) prevent the entry of orders unless there has been compliance with all regulatory requirements that must be satisfied on a pre-order entry basis or if restricted from trading those securities; (iv) restrict access to trading systems and technology that provide access to permit access to persons and accounts that are pre-approved and authorized; and (v) assure that appropriate surveillance personnel receive immediate post-trade execution reports that result from market access. *See* 17 CFR 240.15c3–5(c).

[113] Rule 15c3–5(d) requires the financial and regulatory risk management controls and supervisory procedures to be under the direct and exclusive control of the broker or dealer subject to the requirements of the rule, except under certain proscribed circumstances. Rule 15c3–5(e) imposes certain requirements pertaining to regularly reviewing the effectiveness of the risk management controls and supervisory procedures required by the rule and for promptly addressing any issues. *See* Rule 15c3–5(d) and (e), 17 CFR 242.15c3–5(d) and (e).

[114] The Commission notes that participants that provide sponsored access to SB SEFs would be required to register with the Commission as a broker under Section 15(a)(1) and (b) of the Exchange Act.

[115] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(1) of the Exchange Act).

[116] 15 U.S.C. 78f(b).

[117] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(2)(B) of the Exchange Act).

[118] *See* proposed Rule 810(b)(1).

[119] Section 6(b)(4) of the Exchange Act requires the rules of the exchange to provide for the equitable allocation of reasonable dues, fees, and other charges among its members and issuers and other persons using its facilities. 15 U.S.C. 78f(b)(4).

[120] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(2) of the Exchange Act) and proposed Rule 811(b).

[121] Section 6(b)(5) of the Exchange Act provides, in part, that the rules of the exchange must not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers. 15 U.S.C. 78f(b)(5).

Rule 810(b)(1), proposed Rule 810(b)(2) is designed to support the impartial access requirements of Core Principle 2 and promote fair competition on SB SEFs.

Proposed Rule 810(b)(3) would require a SB SEF to establish rules that promote just and equitable principles of trade.[122] This proposed requirement is comparable to a similar requirement for national securities exchanges contained in Section 6(b)(5) of the Exchange Act.[123] The purpose of proposed Rule 810(b)(3) is to require SB SEFs to design their rules in a manner that advances the goals of the Exchange Act of promoting fair and competitive markets for SB swaps. SB SEFs, by establishing rules for trading and monitoring trading among buyers and sellers of SB swaps on their systems, could play a significant role in the development of regulated markets for SB swaps, which in turn would help reduce incidents of systemic risk.

Finally, proposed Rule 810(b)(4) would require a SB SEF to adopt rules that, in general, would provide a fair procedure for disciplining participants for violations of the rules of the SB SEF.[124] This proposed requirement is analogous to a similar requirement for national securities exchanges in Section 6(b)(7) of the Exchange Act.[125] A SB SEF is required, pursuant to Section 3D(d)(2) of the Exchange Act, to enforce compliance with any of its rules.[126] SB SEFs may choose to enforce rules on their markets by applying penalties and taking other disciplinary actions against participants for violations of their rules. Proposed Rule 810(b)(4) is designed to ensure that, when the SB SEF pursues disciplinary action against a participant for violations of the SB SEF's rules, the participant is afforded a fair process.

While the Commission intends for a SB SEF to retain flexibility in establishing its disciplinary procedures, the Commission anticipates that such rules would have to comply with rules recently proposed under Regulation MC,[127] should those rules be adopted by the Commission. Proposed Rule 702(h) under Regulation MC would require any disciplinary process of a SB SEF to preclude any group or class of participants from dominating or exercising disproportionate influence on the disciplinary process. In other words, to the extent that there is more than one type of group or class of persons that are participants in a SB SEF, the composition of any disciplinary panel or other disciplinary body should not allow one group or class to have representation that is out of proportion in comparison to other groups or classes of persons that are participants in the SB SEF. In addition, any panel or other body that is responsible for disciplinary decisions, and any appellate body for the reviewing of disciplinary decisions, would have to include at least one independent director.[128] The Commission preliminarily believes that proposed Rule 810(b)(4) under Regulation SB SEF would supplement and enhance the proposed requirements of Regulation MC, although the Commission requests comment on the extent to which both sets of rules are necessary to mitigate potential conflicts of interest with respect to the SB SEF's disciplinary process.[129]

Proposed Rule 810(c) would prohibit a SB SEF from using any confidential information it collects or receives, from or on behalf of any person, for non-regulatory purposes. The purpose of proposed Rule 810(c) is to prevent the SB SEF from taking commercial advantage of any confidential information that it receives in connection with its regulatory responsibilities.

The Commission requests comments on all aspects of the proposed Rule 810 implementing Core Principle 1. Are the provisions of proposed Rule 810 appropriate and sufficiently clear? If not, why not and are there preferable alternatives? What are the benefits and drawbacks of imposing on SB SEFs proposed requirements that are comparable to those statutory provisions that are applicable to national securities exchanges under the Exchange Act?

Is the Commission's proposed rule that would require a SB SEF's rules to provide for fees, dues, and other charges that are reasonable and equitably allocated among participants and any other persons using its system appropriate and sufficiently clear? Is this requirement necessary? If not, why not and are there preferable alternatives to help support the statutory goal of impartial access? Are there circumstances under which it would not be appropriate to require the SB SEF to allocate fees, dues, and other charges equitably? In what instances might a SB SEF seek to differentiate among its users with respect to fees, dues, and other charges, including discounts and rebates? Should any of those instances be permitted or restricted?

Is the Commission's proposed rule requiring a SB SEF to establish rules and systems that are not designed to permit unfair discrimination among participants and any other persons using its system appropriate and sufficiently clear? If not, what additional guidelines should the Commission consider for determining when a rule or system would create unfair discrimination among users of the SB SEF's system? What, if any, existing aspects of the current market for SB swaps may lead to unfair discrimination among market participants?

Is the Commission's proposed rule requiring a SB SEF to establish rules to promote just and equitable principles of trade appropriate and sufficiently clear? Are there any specific rules or practices that the Commission should require SB SEFs to adopt for this purpose? If so, what rules or practices, existing or otherwise, should the Commission require? Should the Commission provide guidance on the types of rules that it believes would promote just and equitable principles of trade?

Are there any other requirements that the Commission should impose on a SB SEF to promote fair markets and competition? What factors would most promote fair markets and competition in trading SB swaps, in particular?

Is the proposed requirement that a SB SEF establish a fair procedure for disciplining participants for violations of the rules of the SB SEF appropriate and sufficiently clear? Are there any standards that the Commission should require, at a minimum, for such fair procedures? Is it sufficiently clear how SB SEFs could comply with this requirement in light of the requirements of proposed Rule 702(h) in Regulation MC, which would require the SB SEF to preclude any group or class of participants from dominating or exercising disproportionate influence on the SB SEF's disciplinary process and to have at least one independent director on any disciplinary panel? If not, in what way is the interaction of proposed Rule 810(b)(4) of Regulation SB SEF and proposed Rule 702(h) of Regulation MC unclear and what steps could the Commission take to improve these provisions? Should the Commission provide further guidance on how SB SEFs could establish disciplinary

[122] *See* proposed Rule 810(b)(3).

[123] Section 6(b)(5) of the Exchange Act provides, in part, that the rules of the exchange must be designed to promote just and equitable principles of trade. 15 U.S.C. 78f(b)(5).

[124] *See* proposed Rule 810(b)(4).

[125] Section 6(b)(7) of the Exchange Act requires the rules of the exchange to provide a fair procedure for the disciplining of members and persons associated with members. 15 U.S.C. 78f(b)(7).

[126] 15 U.S.C. 78c–4(d)(2).

[127] *See* Regulation MC Proposing Release, *supra* note 82.

[128] *See* proposed Rule 702(h) under Regulation MC, Regulation MC Proposing Release, *supra* note 82.

[129] For a discussion of further proposals to mitigate conflicts of interest related to SB SEFs, *see infra* Section XVII.

procedures that would comply with the requirements of proposed Rule 810(b)(4) in Regulation SB SEF? Are there additional measures that the Commission should take to foster the independence of the SB SEF's disciplinary process, such as requiring any appeals of disciplinary actions to be considered by the SB SEF's independent directors?

Proposed Rule 810(c) would prohibit SB SEFs from using for non-regulatory purposes any confidential information they collect or receive in connection with their regulatory obligations. Would this proposed rule provide sufficient protection from the improper use of sensitive information by a SB SEF? If not, what other measures should the Commission consider requiring SB SEFs to implement to protect the confidentiality of the non-public information that they collect or receive? Please provide specific suggestions and explain how such suggestions would better address the need to keep non-public information confidential.

VIII. Core Principle 2—Compliance With Security-Based Swap Execution Facility Rules

Section 3D(d)(2) of the Exchange Act (Core Principle 2) states that a SB SEF shall: (A) Establish and enforce compliance with any rule established by such SB SEF, including (i) the terms and conditions of the SB swaps traded or processed on or through the facility and (ii) any limitation on access to the facility; (B) establish and enforce trading, trade processing, and participation rules that will deter abuses and have the capacity to detect, investigate, and enforce those rules, including means (i) to provide market participants with impartial access to the market and (ii) to capture information that may be used in establishing whether rule violations have occurred; and (C) establish rules governing the operation of the facility, including rules specifying trading procedures to be used in entering and executing orders traded or posted on the facility, including block trades.[130] The Commission is proposing to implement these statutory requirements in proposed Rule 811(a) of Regulation SB SEF.

The Commission believes that the primary issues raised by this Core Principle relate to the rules that a SB SEF must establish and enforce regarding access, the SB swaps that could trade on the system, and surveillance, investigation and enforcement of participants' activities on the SB SEF. In proposing Rule 811(a) of Regulation SB SEF to implement this Core Principle, the Commission has been informed by its experience with regulating both national securities exchanges and ATSs, while recognizing that differences exist between the cash equities and listed options markets and the market for SB swaps.

Much as Sections 6 and 19 of the Exchange Act[131] require that national securities exchanges have rules, among other things, to govern trading, membership, and discipline of its members, the Commission preliminarily believes that, pursuant to Section 3D(d)(2) of the Exchange Act, SB SEFs should have similar rules. In this way, participants would be fully informed of the rules governing various aspects of the operation of the SB SEF and the requirements governing trading on the system, and would recognize that there would be consequences if they fail to comply with those rules. Below is a discussion of the rules that, in the Commission's view, would need to be developed and implemented by SB SEFs to comply with Core Principle 2. These proposed rules are not meant to be an exhaustive list, and the Commission believes that a SB SEF would need to evaluate its own market to determine the measures that are necessary to implement the Core Principles.

A. Denials or Limitations on Access

Core Principle 2 is in part concerned with limitations on access and mandates that SB SEFs provide impartial access to their markets.[132] The Commission discusses the substantive issues relating to access, and the rules it is proposing relating to access, in Section VI above.[133] The Commission believes that one of the most important requirements of Core Principle 2 concerns the SB SEF's rules regarding impartial access to the facility. The Commission discusses the procedural rules it is proposing in connection with the Core Principle 2 requirement for impartial access below. As the Commission noted in the Regulation MC Proposing Release, participants of a SB SEF might seek to limit the number of direct participants of the SB SEF to limit competition and increase the opportunity for higher profit margins.[134]

The Commission is proposing several procedural rules in support of the proposed requirements for impartial access discussed above in Section VI. First, proposed Rule 811(b)(3) would require every SB SEF to make and keep records of all grants of access, including, for all participants, the reasons for granting such access, and all denials or limitations of access, including, for each applicant, the reasons for denying or limiting access. The purpose of proposed Rule 811(b)(3) is to ensure that Commission staff would have the ability to examine such records upon request, pursuant to the requirements of proposed Rule 814 of Regulation SB SEF.[135] In addition, proposed Rule 811(b)(4) would require each SB SEF to file notice with the Commission (by filing an annual amendment to proposed Form SB SEF[136] and in the compliance report required of the CCO pursuant to Core Principle 14 and proposed Rule 823 of Regulation SB SEF), if the SB SEF prohibits or limits access to the facility for any participant, or if the SB SEF denies access to an applicant.[137] In its notice, a SB SEF should inform the Commission of the reasons for its denial of access and provide the Commission with the contact information of the aggrieved participant or applicant.[138] Together, these requirements, which would provide the Commission with information about, or access to information about, any instances when the SB SEF has denied access to a participant or an applicant to become a participant, should help the Commission carry out its oversight of SB SEFs. This ability is particularly important given the identified potential

[130] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(2) of the Exchange Act).

[131] *See, e.g.,* Sections 6(b) and 19(g) of Exchange Act, 15 U.S.C. 78f(b) and 78s(g).

[132] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(2)(A)(ii) and 3D(d)(2)(B) of the Exchange Act).

[133] *See supra* Section VI, notes 79 to 114.

[134] *See* Regulation MC Proposing Release, *supra* note 82. *See also infra* Section VI. As discussed further in Section XVII below, the Commission proposed a number of requirements in Regulation MC designed to mitigate potential conflicts of interest relating to SB SEFs, as discussed in the Regulation MC Proposing Release. The additional rules the Commission is proposing herein relating to impartial access are designed to work together with proposed Regulation MC to help mitigate potential conflicts of interest, as identified in the Regulation MC Proposing Release. In addition, as discussed in Section XVII, the Commission is proposing governance rules that also are designed to help mitigate potential conflicts of interest relating to SB SEFs.

[135] *See infra* Section VI discussing proposed Rule 814 regarding the Commission's ability to obtain information.

[136] *See infra* Section XXII discussing proposed Form SB SEF. The Commission notes that proposed Form SB SEF would be a publicly available document, and so such notice would be publicly available.

[137] *See infra* Sections XXIII and XXI for a discussion of Form SB SEF and the responsibilities of the CCO, respectively.

[138] The Commission could bring an enforcement action if it believed that a SB SEF had denied or limited access in contravention of the Exchange Act and the rules thereunder.

conflict of interest concerns with respect to access to a SB SEF.[139]

Further, under proposed Rule 811(b)(5), a SB SEF would be required to establish a fair process for the review of any prohibition or limitation on access with respect to a participant or any refusal to grant access with respect to an applicant.[140] Fair access to trading venues for SB swaps, and consequently a fair review process, is important, especially when a SB SEF may be the only venue for the trading of a particular SB swap. The Commission believes that for any such review process by a SB SEF to be fair, at a minimum, those persons involved in the decision to prohibit, limit, or deny a participant's or applicant's access to the SB SEF should not be involved in the review of whether such prohibition, limitation, or denial was appropriate. Otherwise, the purpose of the review process could be undermined. The SB SEF's Board should consider the most appropriate body to conduct the internal review process, whether that body is the Board itself, a committee that is delegated this function by the Board, or some other appropriate body.

The Commission requests comment on all aspects of its proposal regarding denials or limitations of access. Is the proposed rule requiring a SB SEF to notify the Commission annually of any prohibition, limitation, or denial of access to its services appropriate and sufficiently clear? Would this be useful information for market participants and the public? Should the Commission require notice more often than annually? Would the proposal assist in mitigating conflicts of interest on the part of a SB SEF? If so, how so? If not, why not?

Is the Commission's proposed rule regarding a SB SEF's review of its denials of access appropriate and sufficiently clear? If not, why not and what would be a better approach? Are there any measures that the Commission could require that would result in a more meaningful internal review process? For example, should the Commission explicitly require that the Board or the regulatory oversight committee ("ROC") review all denials of or limitations on access?[141] Would such a proposal be useful? If so, within what time frame should the review be completed? Are there any other requirements the Commission should impose?

B. Swap Review Committee

Proposed Rule 811(c) would require a SB SEF to establish and enforce compliance with rules concerning the terms and conditions of the SB swaps traded on the facility. To carry out this requirement, a SB SEF would be required to establish a swap review committee[142] to determine the SB swaps that trade on the SB SEF, as well as the SB swaps that should no longer trade on the SB SEF. The proposed rule would require that the composition of the swap review committee provide for the fair representation of participants in the SB SEF and other market participants. Specifically, the proposed rule would require that each class of participant and other market participants (such as the customers of participants, including end-users and buy-side firms) would have the right to participate in the swap review committee. The proposed rule also would provide that the members of the swap review committee be chosen so that no single class of participant or category of market participant would predominate. The rules of the SB SEF also would be required to stipulate the method by which such representation would be chosen by the Board of the SB SEF.[143] Having a compositionally balanced committee should help to assure that the process of determining those SB swaps that should trade (or no longer should trade) would be fair and that various classes of participants in the SB SEF, as well as other market participants, would have a voice in those decisions.

Proposed Rule 811(c)(3) would require the SB SEF to establish criteria to be used by the swap review committee in determining which SB swaps should be traded on the SB SEF. The Commission preliminarily believes that this would allow the most flexibility by permitting a SB SEF to choose whatever criteria it believes are important in determining which SB swaps to trade, thereby encouraging as much trading of SB swaps on SB SEFs as possible.

The Dodd-Frank Act requires that transactions involving SB swaps subject to the clearing requirement of subsection (a)(1) of Section 3C of the Exchange Act be executed on an exchange or on a registered SB SEF unless no exchange or SB SEF makes the SB swap available to trade.[144] Consequently, once a SB swap is "made available to trade" on an exchange or a SB SEF (and is required to be cleared), it can no longer trade in the OTC market, making the determination of what it means for a SB swap to be "made available to trade," as well as the decision as to who makes such a determination, central to the implementation of Title VII of the Dodd-Frank Act. The Commission has received comments that the scope of those SB swaps that are made available for trading would be important in this market because of the mandatory trade execution requirement and the nature of the SB swap market,[145] which is relatively illiquid and has a smaller number of market participants in comparison to the cash equities and listed options markets.[146]

In the Regulation MC Proposing Release, the Commission identified conflicts of interest that could arise when a small number of market participants exercise control or undue influence over a SB SEF.[147] When trading of SB swaps is dominated by a small number of participants, those

[139] *See* Regulation MC Proposing Release, *supra* note 82.

[140] *See* proposed Rule 811(b)(5). Such a process is required for all national securities exchanges and for ATSs that have exceeded certain volume thresholds. *See* Sections 6(c) and 19(e) of the Exchange Act (15 U.S.C. 78f(c) and 78s(e)) and Rule 301(b)(5) (17 CFR 242.301(b)(5)) of Regulation ATS.

[141] The Commission proposed in Regulation MC to require a SB SEF to have a ROC, and that the ROC be composed of independent directors. *See* Regulation MC Proposing Release, *supra* note 82.

[142] The swap review committee would not be required to be a committee of the Board under the Commission's proposed rule, although a SB SEF may choose to allow or require members of its Board to serve on the swap review committee, as the SB SEF would determine.

[143] *See* proposed Rule 811(c)(2).

[144] *See* Section 3C(h) of the Exchange Act. The requirement in Section 3C(h) of the Exchange Act that a SB swap that is made available to trade on an exchange or a SB SEF shall be traded on an exchange or SB SEF (and not in the OTC market) only applies to SB swaps subject to mandatory clearing. Section 3C(h) of the Exchange Act generally states that, with respect to transactions involving SB swaps subject to the clearing requirement of paragraph (a)(1) of Section 3C, counterparties shall: (1) Execute the transaction on an exchange; or (2) execute the transaction on a registered SB SEF or a SB SEF that is exempt from registration. However, these requirements shall not apply if no exchange or SB SEF makes the SB swap available to trade or for SB swap transactions subject to the clearing exception in paragraph (g) of Section 3C.

In a separate proposed rulemaking, the Commission, among other matters, is seeking comment generally on how the factors identified in the statute relating to the mandatory clearing requirement should be applied in making determinations as to whether particular SB swaps are or should be required to be cleared. *See* Securities Exchange Act Release No. 63557 (December 15, 2010), 75 FR 82490 (December 30, 2010) (File No. S7–44–10).

[145] *See, e.g.,* Commentary by Yves P. Denizé, Director & Associate General Counsel, TIAA–CREF, at the Roundtable. Webcast available at *http://www.sec.gov/news/openmeetings/2010/jac091510.shtml.*

[146] The market for SB swaps today is concentrated in the hands of a few dealers. *See supra* note 81, stating that five large commercial banks represent 97% of the total banking industry notional amounts.

[147] *See* Regulation MC Proposing Release, *supra* note 82, 75 FR at 65890.

participants may have competitive incentives to, among other things, limit the number of SB swaps that are made available for trading by a SB SEF to keep those SB swaps trading in the OTC market. This could be true even for SB swaps that would have sufficient trading activity to trade on a SB SEF.[148] On the other hand, once the determination has been made that a SB swap that is subject to mandatory clearing is available to trade on an exchange or a SB SEF, then such SB swap can no longer trade in the OTC market, even if trading of the SB swap on the exchange or SB SEF were virtually nonexistent. Thus, a determination by even one SB SEF or national securities exchange that a SB swap was available to trade on the exchange or SB SEF could have unintended consequences for the trading of such SB swap.

In light of these competing incentives stated above, the Commission preliminarily believes that it would be appropriate that the decision as to when a SB swap would be considered to be "made available to trade" on an exchange or a SB SEF pursuant to Section 3C(h) of the Exchange Act should be made pursuant to objective measures established by the Commission, rather than by one or a group of SB SEFs. Such objective measures could provide that a SB swap that is subject to mandatory clearing would be "made available to trade" unless the SB swap fails to meet a threshold test that the Commission may adopt or, conversely, that no SB swap would be "made available to trade" unless the SB swap passed a threshold test that the Commission may adopt. In either case, under this approach the Commission would in effect interpret the phrase "made available to trade" in Section 3C(h) of the Exchange Act as meaning something more than the decision to simply trade, or essentially list, a SB swap on a SB SEF or an exchange.[149] This approach would have the further effect of permitting SB swaps to be made subject to mandatory clearing independently of whether they are required to be traded exclusively on SB SEFs and exchanges, because there would not be an automatic requirement that SB swaps subject to mandatory clearing trade only on a SB SEF or exchange simply because they are listed on one.

The Commission does not, however, have sufficient data at this time to propose the objective standards pursuant to which a determination whether a SB swap is "made available to trade" would be made. The Commission preliminarily anticipates that it will separately address how to determine when a particular SB swap would be considered to be "made available for trading" on an exchange or SB SEF pursuant to the directive of Section 3C(h) of the Exchange Act. We solicit comment in this release, however, on how the Commission should craft an objective standard for whether a SB swap is "made available to trade." For example, an objective determination could be based on a formula measuring the percentage of trading in a particular SB swap that was taking place on exchanges and SB SEFs compared to the aggregate percentage of trading that was taking place in the SB swap on exchanges and SB SEFs, and in the OTC market.[150] Alternatively, such a determination could be based on overall volume in the SB swap, wherever executed. In addition, such a test could require that a baseline trading threshold for each SB swap be met. For example, such a threshold could be that, within a given measurement period, a minimum number of transactions in the SB swap be executed or that a minimum notional value in the SB swap be traded. There may be instances when, because of a low total number of transactions in a SB swap, it may not be appropriate to determine that such SB swap should be made available to trade.

It also may be appropriate to utilize objective measures to determine when a SB swap should no longer be considered to be made available for trading. If it were determined that a SB swap should no longer be considered to be made available for trading because, for example, among other objective measures very little trading in such SB swap on SB SEFs has occurred over a specified time period, such SB swap would be able to trade in the OTC market, as well as on exchanges and SB SEFs.

Proposed Rule 811(c)(4) would require the swap review committee to periodically review each SB swap trading on the SB SEF to determine whether the trading characteristics of each such SB swap justify a change to the trading platform being used for that particular SB swap. In making such a determination, the swap review committee would need to consider whether (1) the liquidity in each SB swap is at an appropriate level for the SB swap's trading platform on which it trades; and (2) such SB swap would be more suited for trading on a different type of platform, including a platform that provides for increased price transparency for participants entering quotes, orders, or other trading interest. The first review could not be earlier than 120 days after the initiation of trading for a given SB swap.

Proposed Rule 811(c)(4) is designed to ensure that SB swaps that are trading on the SB SEF are trading on an appropriate platform. For example, if a SB swap is trading in an RFQ mechanism but trading in the SB swap becomes sufficiently liquid, the SB SEF should consider moving the SB swap to a platform with greater transparency. There could be reasons why the SB SEF prefers not to do so, *e.g.,* because the predominant dealers on the market prefer to continue trading the SB swap in the RFQ platform that does not have the same degree of transparency and thus competition, as a limit order book. Having such decisions made by the swap review committee, and reported promptly to the CCO and annually to the ROC and the Board (as discussed in the next paragraph), appear to lessen any undue influence that any one class of participants may have in keeping the SB swap trading on a platform that does not afford the appropriate level of price transparency for that SB swap.

Proposed Rule 811(c)(5) would require the swap review committee to report decisions on each SB swap promptly to the CCO and annually to the ROC. This would include initial decisions on trading SB swaps as well as ongoing determinations pursuant to the reviews of the swap review committee. This would help ensure that the CCO is kept apprised of changes in the trading of SB swaps so that trading can be properly monitored.

The Commission requests comment on all aspects of the rules relating to the swap review committee and its responsibilities. Is the Commission's proposed rule concerning the composition of the swap review committee appropriate and sufficiently clear? Should the Commission's rule contain more detail about the requirements for the composition of the committee? If so, what should those requirements be? Should the

[148] *Id.*

[149] Pursuant to proposed Rule 811(c), the swap review committee of each SB SEF would be responsible for determining which SB swaps the SB SEF permits to be traded on the SB SEF. Under the proposed approach, however, this decision would not be the same as a determination that such SB swap had been made available for trading within the meaning of Section 3C(h) of the Exchange Act. The swap review committee's decision, therefore, would not in and of itself be the sole determinant of when a SB swap could no longer trade in the OTC market.

[150] Because all SB swap transactions would be required to be reported to a registered SDR, whether they occur on an exchange, a SB SEF, or in the OTC market, the Commission would have access to complete information on trading volume regarding each SB swap.

Commission require independent director representation on the swap review committee?

Is the Commission's proposed Rule 811(c)(3) concerning how the SB SEF should determine whether to trade a SB swap appropriate and sufficiently clear? Should the Commission include any particular factors that the SB SEF should consider, and, if so, what should those factors be and why?

As discussed above, under the proposal the Commission would interpret the phrase "made available to trade" in Section 3C(h) of the Exchange Act as meaning something more than the decision to simply trade, or essentially list, a SB swap on a SB SEF or an exchange. The Commission requests comment on whether commenters agree with this approach, or if, instead, we should consider a SB swap to be "made available to trade" if it is listed on an exchange or a SB SEF in compliance with applicable rules and regulations. What are the advantages and disadvantages of such an approach? Would the approach be more or less simple and cost-effective than the proposal, which would involve the Commission in determining whether a SB swap is "available to trade" and distinguishes this from the determination under proposed Rule 811(c)(3) of whether a SB swap should be traded or listed on a SB SEF? Does the review under proposed Rule 811(c)(3) accomplish many or all of the Commission's regulatory objectives? Would an approach that deems a SB swap "available to trade" if it is listed be more or less susceptible to manipulation or gaming than the proposed approach? Would an approach that deems a SB swap "available to trade" if it is listed generally result in more or less trading of SB swaps on exchanges or SB SEFs? If the Commission were to take the position that listing of a SB swap on an exchange or a SB SEF is the same as "made available to trade," could the Commission's potential concerns about permitting SB SEFs and exchanges to determine whether a SB swap is "available to trade" be addressed through an exemptive process that could consider potential adverse effects or unintended consequences as to particular SB swaps? Are the Commission's potential concerns about permitting SB SEFs and exchanges to determine whether a SB swap is "available to trade" affected by the types of trading permitted on a SB SEF, such as the ability to send an RFQ to only one or few other participants? If the Commission were to take the position that listing of a SB swap on an exchange or SB SEF is the same as "made available to trade," the Commission could subject SB swaps to mandatory clearing independently of whether such SB swaps are required to be traded on SB SEFs or exchanges by, for example, using an exemptive process or specifying, at the time the mandatory clearing determination is made, that a SB swap is not "available to trade" unless certain criteria are met. What would be the advantages and disadvantages of such an approach compared to the Commission's proposal?

The Commission requests comment on whether it would be appropriate for the decision as to when a SB swap would be considered to be "made available to trade" on an exchange or a SB SEF pursuant to Section 3C(h) of the Exchange Act to be made pursuant to objective measures established by the Commission, rather than by one or a group of SB SEFs. If not, why not? If not, is there another method that commenters would suggest, other than having the determination made by SB SEFs? If so, what is that method?

The Commission requests comment on the manner in which the determination to make a particular SB swap available for trading would be made. What would be an appropriate method or standards to determine whether a SB swap should be made available for trading? Should the test be based on the aggregate amount of trading in the SB swap on exchanges and SB SEFs and in the OTC market, or on overall volume, wherever the SB swap may be executed? What would be an appropriate volume threshold for each alternative, and why? Should a volume threshold vary by asset class? Is one test more appropriate for some asset classes and the other test more appropriate for others? If so, why, and what is the appropriate volume threshold for each asset class with each test? What would be the appropriate measurement period for a volume threshold and why? On what other characteristics could the test be based? Frequency of trading? The number of SB SEFs on which the SB swap is also trading?

Should there be some minimum level of liquidity in both the OTC market and on SB SEFs and exchanges in connection with the determination that a SB swap has been made available to trade? If so, what is the appropriate level of liquidity? What is a baseline threshold that SB swaps made available to trade should meet? Should it be based on the number of transactions, the notional value for a given SB swap, or both, over a set time period? Or, is there another baseline threshold that the Commission should consider? If so, what is it? Over what time period should the activity be measured?

What would be an appropriate test to determine that a SB swap should no longer be considered to be made available for trading? Because such a SB swap would not be trading in the OTC market, a volume test similar to one of the suggested tests above to determine whether a SB swap should be considered to be made available for trading—comparing the aggregate percentage of trading on exchanges and SB SEFs to overall trading—may not be feasible. How little trading on SB SEFs should be taking place before the Commission determines that the SB swap should be permitted to trade again in the OTC market (because it is no longer considered to be "made available for trading")? Is there a specific number of trades that would make it appropriate to determine that a SB swap is no longer considered to be made available for trading? If so, what should that number be? Or, should a test be based on a percentage trading volume comparison of trading activity in a SB swap to a time period prior to when it was considered to be made available to trade? What period of time would be appropriate to determine if a pattern of lack of trading has set in? Should such a determination be based on a test based on something other than trading volume? If so, what should such a test be? How should the Commission take into account the possibility that market participants might engage in gaming behavior to affect the outcome of a test based on trading frequency or volume?

Should the presumption be that no SB swap is deemed made available to trade unless it meets the threshold established by any test that the Commission may adopt, or should the presumption be that all SB swaps are deemed available to trade unless they fail to meet the threshold established by any such test? What would be the costs and benefits of each approach?

Has the Commission correctly identified the potential conflicts with SB SEFs that could arise in decisions to make a SB swap available to trade? Would the proposal the Commission has outlined here help to mitigate those conflicts? If not, why not?

How, if at all, would having the determination about what SB swaps are made available for trading be made pursuant to an objective formula, as the Commission is considering to propose, rather than allowing each SB SEF to make the determination, impact the incentives for creating a SB SEF? Would the proposal have the effect of chilling the creation of SB SEFs because trading

could simply continue in the OTC market until trading meets the objective test? If so, how should the determination of what is made available to trade be made? How should the Commission guard against the concern that, if a distinction is not made between "listing" or "trading" of a SB swap, and "making available to trade," OTC trading could effectively be cut off in SB swaps that were made available to trade, even if market participants believe that they would benefit from continued OTC trading? Is this concern mitigated if the Commission adopts an interpretation of the definition of SB SEF that permits an RFQ to be sent to only one other participant? Why or why not? Under such approach, would there still remain benefits for the OTC trading of certain types of SB swaps by market participants? If so, what would be these benefits and under which circumstances, and for what types of SB swaps, would this be the case? How should those benefits, if any, be weighed with the Dodd-Frank Act's goal of moving trading in SB swaps onto regulated markets?

Would the idea of looking at volume trading on SB SEFs and SBS exchanges versus trading in the OTC market be subject to gaming? For example, would it be possible for firms to avoid having SB swaps designated as made available to trade, for example, by suppressing SB SEF trading volume by posting inferior quotes on SB SEFs while continuing to offer the identical product in the OTC market at a better price? If so, what impact would such behavior have on the SB swap market? If so, how could the Commission guard against such behavior?

If the Commission has not adopted a standard for determining when a SB swap is made available to trade by the time a SB swap is determined to be subject to mandatory clearing, what action, if any, should the Commission take to clarify the impact of a SB SEF or exchange listing a SB swap for trading on its market? Would it be necessary or appropriate for the Commission to clarify the meaning of "made available to trade" in these circumstances and, if so, what type of clarification should the Commission provide? Commenters should address the impact, if any, of any action or inaction by the Commission in these circumstances on market participants and on the trading of SB swaps, including the impact of any clarifications that commenters may propose.

Is the Commission's proposed Rule 811(c)(4) requiring review by the swap review committee of the liquidity of SB swaps, and its potential requirement for an SB SEF to move trading of the SB swap to a different type of platform operated by the SB SEF that would provide for greater pre-trade price transparency, once certain volume thresholds are met, sufficiently clear? Is it necessary for a swap review committee to review SB swaps trading on limit order book platforms, as well as multiple dealer RFQ platforms? If not, why not? Should the Commission establish a trading activity threshold that, if exceeded, would require a SB SEF to move the trading of SB swaps to a limit order book platform? If so, what would be the appropriate factors and threshold? For example, should such factors include the liquidity of the SB swap? If so, how should such liquidity be measured (*e.g.,* average daily trading volume, frequency of trades, size of trades)? What would be an appropriate measurement period for any such threshold(s)? Should a threshold vary depending on the type of SB swap? Should a threshold be relative (*e.g.,* based on a specified percentage of overall volume) or absolute (*e.g.,* based on a specific number of trades in a given measurement period)? What are the benefits and drawbacks of mandating a trading activity threshold that, if exceeded, would require a SB SEF to move the trading of SB swaps to a limit order book platform?

C. Trading Procedures

Proposed Rule 811(d) would require every SB SEF to establish and enforce rules governing the procedures for trading on the SB SEF, including but not limited to: doing business on the SB SEF; types of orders or other trading interest available; the manner in which trading interest would be handled on the SB SEF, including a proposed requirement that the rules provide for the fair treatment of all trading interest; the manner in which price transparency for participants entering orders, requests for quotations, responses, quotations, or other trading interest into the system would be promoted; the manner in which trading interest, including orders, requests for quotations, responses, quotations, and transaction data, would be disseminated, including whether dissemination would be only to participants of the SB SEF or more broadly, and whether or not for a fee; prohibited trading practices; the handling of clearly erroneous trades; trading halts; the manner in which block trades would be handled, if different from the handling of non-block trades; and any other rules concerning trading on the facility. The Commission believes that it is important for a SB SEF to have rules concerning doing business on the SB SEF because such rules would provide participants with a uniform set of expectations for how the SB SEF would operate.

The Commission expects that such rules would include information as basic as the hours the SB SEF is available for trading, as well as rules concerning the manner in which trading interest would be handled by the SB SEF. Such rules also would help to inform participants as to the types of orders or other trading interest that they could enter into the system for execution. The Commission also believes that rules concerning prohibited trading practices would be important to every SB SEF, so that participants would be aware of the scope of allowable behavior on the SB SEF. Such rules would help to support the requirement in Core Principle 2 that every SB SEF would have to establish rules that would deter abuses and have the capacity to detect, investigate and enforce those rules.

The Commission believes that it is important to the efficient trading on a SB SEF that the SB SEF provide for the fair treatment of all trading interest on its market. In other words, a SB SEF should have rules designed to enhance liquidity, including rules that are not designed to disadvantage participants' orders, thereby causing them to miss out on trading opportunities. Such rules might include, for example, price/time priority or price/size priority rules.[151] The SB SEF would need to apply these rules consistently and fairly with regard to all participants.

In addition, as discussed in Section III above, the Commission believes that transparency of prices on a SB SEF is a critical element with respect to the operation of a SB SEF. Although the Commission is not proposing to dictate a certain type of trading system or trading rules for SB SEFs, it believes that a SB SEF would have to meet certain basic standards to comply with the requirements that its rules provide for the fair treatment of all trading interest and that these rules address the manner in which price transparency for participants entering trading interest into the system would be promoted. In this regard, under its proposed interpretation of the definition of SB

[151] Generally, when orders are filled in price/time priority, if there are two orders at the same price, the order that arrived first would be given priority. Alternatively, size may be used to determine priority among trading interest at the same price. For example, orders may be filled pro-rata, or in certain proportions based on other factors the SB SEF may determine are appropriate. *See, e.g.,* International Securities Exchange Rule 713, Priority of Quotes and Orders.

SEF, if the SB SEF operates a RFQ or similar trading model, the rules of the SB SEF should include a functionality that allows the quote requesting participant to submit a RFQ to all participants that are willing to respond to requests, *i.e.,* those participants willing to provide liquidity. The SB SEF, however, could determine to provide the functionality for the requesting participant to choose to send the RFQ to less than all other participants at the request of its customer or when the participant is exercising investment discretion. In addition, the requestor would be able to determine to whom to send the RFQ.

Further, for example, if the SB SEF operates a RFQ mechanism, the rules of the SB SEF should specify that any response to an RFQ that is provided to the participant submitting the RFQ should be included in the composite indicative quote of the SB SEF.[152] In addition, if a SB SEF displays firm, executable trading interest, it must display such interest to all participants.

The Commission believes that it is important to foster pre-trade transparency to encourage greater price competition. However, the Commission is cognizant of comments received from market participants in the SB swap market, both from customers ("buy-side") and liquidity providers ("sell-side"), who are concerned about the level of pre-trade price transparency that may be required. Some of these commenters have expressed the concern that pre-trade price transparency could potentially have an impact on dealers' incentives or ability to provide competitive prices if others can use the information that would be made available through increased pre-trade price transparency to trade ahead of the order. The proposed rules relating to the dissemination of trading interest are designed to increase transparency from current levels, while at the same time recognizing the concerns that have been voiced about the potential effects of pre-trade transparency in certain circumstances. In this regard, proposed Rule 811(d)(5) has been drafted to allow maximum flexibility by a SB SEF to determine the best manner to disseminate trading interest by such SB SEF. The Commission believes that it is important for a SB SEF to make clear to its participants, in a rule, how trading interest would be disseminated. At the same time, the Commission recognizes that different platforms may require different means of disseminating trading interest, and that each SB SEF is in the best position to determine how such dissemination should occur on its own platform. In particular, the Commission believes that proposed Rule 811(d)(5) would require a SB SEF to develop rules that would incorporate responses received on an RFQ system into a composite indicative quote that is available to all participants, and that would not limit the number of dealers from whom a participant could request a quote.

The Commission also believes that SB SEFs should have rules that concern any prohibited trading practices. A SB SEF should determine those trading practices that it believes are inappropriate to the functioning of its market.

The Commission also believes that a SB SEF should have rules concerning the handling of clearly erroneous trades, and that those rules should provide for a fair and nondiscriminatory manner of handling such trades, as well as a procedure to resolve any resulting disputes. Although under ordinary circumstances trades that are executed between parties should be honored, the Commission believes that clearly erroneous execution rules are necessary because, on rare occasions, the terms of the executed trade may indicate that an obvious error may exist. In such instances, it could be unrealistic to expect that the parties to the trade had come to a meeting of the minds regarding the terms of the transaction. In such case, a clearly erroneous transaction may have taken place. The Commission believes that any clearly erroneous execution rule should provide for a clear and transparent process for resolving erroneous trades and for a fair process for hearing appeals of clearly erroneous decisions.

The Commission further believes that it is critical for a SB SEF to have rules concerning trading halts, so that trading on the SB SEF would not continue when trading has been halted or suspended in the underlying security or securities pursuant to the rules or an order of a regulatory authority with authority over the underlying security or securities.[153] The Commission believes that when trading has been halted on an underlying security, it is appropriate that derivative markets, such as the options markets and the SB swap market, also halt trading to avoid inefficient pricing and disruptions to the market.

Core Principle 2 requires that SB SEFs establish (and have the capability to enforce) rules regarding trading procedures. The items enumerated in proposed Rule 811(d) are not meant to be an exhaustive list of rules relating to trading procedures and SB SEFs may put in place additional types of categories of rules that they deem to be necessary to govern the procedures for trading on the SB SEF. The Commission preliminarily believes that each SB SEF would be in the best position to determine precisely those rules that are necessary and appropriate to ensure that its market functions in a fair and orderly fashion. The rules of each SB SEF would be required to be filed as part of the initial Form SB SEF application, as well as in connection with the rule filing process in proposed Rules 805 and 806 of Regulation SB SEF.[154]

The Commission requests comment on all aspects of proposed Rule 811(d). What are commenters' views on the proposed rules relating to trading procedures? Are the Commission's proposed rules concerning trading procedures, the need to promote pre-trade price transparency (proposed Rule 811(d)(4)) and the rule concerning dissemination of trading interest (proposed Rule 811(d)(5)) sufficiently clear? Would proposed Rule 811(d)(4) make a difference in price transparency in the SB swap market? How would it impact behavior? Are there any specific concerns with this proposed rule? If so, what are they? Should the proposed rule be refined? If so, how? Please provide specific suggestions.

What are commenters' views on the proposed requirement that responses to an RFQ must be included in the SB SEF's composite indicative quote? Would this requirement in fact promote pre-trade price transparency? What would be the benefits and drawbacks of the Commission's proposal to include RFQ responses in the composite indicative quote? Should the Commission instead require that only the response to an RFQ accepted by the party submitting the RFQ be included in a composite indicative quote? Should the Commission require that any participant responding to an RFQ have

[152] The composite indicative quote screen would be the quote screen available to all participants of the SB SEF. The composite quote shows an average quote for each SB swap available on the SB SEF. The composite indicative quote includes both composite indicative bids and composite indicative offers. As discussed below, proposed Rule 811(e) would require a SB SEF that operates a RFQ platform to create and disseminate through the SB SEF a composite indicative quote for SB swaps traded on or through the SB SEF and to make that screen available for viewing by all participants in the SB SEF.

[153] The Commission notes that the options and securities futures markets have rules providing for a trading halt in the event that the underlying security has been paused in the equity markets. *See, e.g.* Chicago Board Options Exchange Rule 43.4(b).

[154] *See infra* Section XXIII for a discussion of the proposed rule filing process for SB SEFs.

the ability to see other participants' responses? Would such a requirement make a difference with respect to pre-trade price transparency? What would be the benefits and drawbacks of such a proposal? Should the Commission require that all requests for quote be shown to all participants? Would such a requirement make a difference with respect to pre-trade price transparency? What would be the benefits and drawbacks of such proposals?

Should the Commission require a SB SEF to have a rule prohibiting the SB SEF from disclosing to any liquidity provider that has received an RFQ information about how many participants were queried? What would be the impact of such a prohibition, taking into account such factors as the type of SB swap and the size of the transaction, on the liquidity provider's incentives in determining at what price to provide a response? Should the participant submitting the RFQ be able to waive any such prohibition in the exercise of its investment discretion?

For SB SEFs that choose to allow trading of uncleared SB swaps should the Commission require such SB SEFs to have additional trading rules related to uncleared SB swaps, such as rules for disclosing the counterparties to such transactions or other rules related to counterparty risks? Please provide specific suggestions.

Proposed Rule 811(e) would require a SB SEF that operates an RFQ platform to create and disseminate through the SB SEF a composite indicative quote for SB swaps traded on or through the SB SEF.[155] The composite indicative quote would need to be made available to all participants of the SB SEF. The composite indicative quote would include both composite indicative bids and composite indicative offers. The Commission preliminarily believes that a composite indicative quote would provide valuable pricing information to the participants of a SB SEF, while at the same time not disclosing specific trading interest of individual participants when that interest is not firm. As discussed above, the Commission believes that including responses to an RFQ in the composite indicative quote also may be appropriate as a means to further increase pre-trade price transparency. A composite indicative quote would provide some information on pricing but would take into account concerns expressed by some market participants about information leakage that could occur, particularly with respect to larger sized orders.[156] In addition, the Commission understands that many platforms operating today in the SB swaps market create and disseminate a composite indicative quote.

The Commission requests comment on all aspects of proposed Rule 811(e). What are commenters' views on the proposed requirement that a SB SEF must disseminate a composite indicative quote? What would be the benefits or drawbacks of such a proposal? Would such a requirement provide an increased level of pre-trade price transparency compared to the level that is available today? Are there other measures the Commission should impose at this time to foster pre-trade price transparency? If so, what are they? For example, should the Commission require a SB SEF to provide functionality to enable market participants to post individual indicative quotes, in addition to a composite indicative quote? What would be the advantages and disadvantages of such a proposal?

Considering the early stage of development of the regulatory framework for the SB swap market and the existing structure of the SB swap market, the Commission is mindful that its interpretation of the definition of SB SEF, and the rules it is proposing herein to implement the Dodd-Frank Act, could have unforeseen consequences, either beneficial or undesirable, with respect to the shape that this market will take. In the Commission's view, it is important that the regulatory structure will provide incentives for the trading of SB swaps on regulated markets that are designed to foster greater transparency and competition that are subject to Commission oversight, while at the same time allowing for the efficient operation and continued evolution of the SB swap market. With that in mind, should the Commission mandate greater pre-trade price transparency at the outset of trading of SB swaps on SB SEFs? What would be the benefits of mandating greater pre-trade price transparency at the start of trading of SB swaps on a SB SEF and what would be the drawbacks of such an approach? Would the benefits outweigh the drawbacks and vice versa? Commenters should explain their reasoning. Should the Commission propose additional trading rules to be required of SB SEFs? If so, what should those rules cover with regard to trading procedures?

D. Block Trades

Core Principle 2 requires a SB SEF to establish rules governing the operation of the facility, including rules specifying trading procedures to be used in entering and executing orders traded or posted on the facility, including block trades.[157] The issue of block trades on a SB SEF has two components: (1) How should a "block trade" be defined, *i.e.,* at what threshold would a trade be considered block size; and (2) how should block trades be handled on a SB SEF. Issues relating to the execution, as well as the reporting, of a block trade, have been a particular focus of market participants. Market participants that execute block trades in SB swaps, including dealers and buy-side customers, have raised concerns regarding pre-trade transparency of block trades. They believe that if other market participants know the terms of a block trade prior to the time it is executed, those other market participants could attempt to profit from the information about the block to the detriment of the initiator of the block trade. If the information is disclosed before the block trader's liquidity provider is "on risk," other market participants could buy or sell ahead of the block trade initiator, moving the market against the block trade initiator (but not adversely affecting its counterparty). If the liquidity provider for the block trade initiator is "on risk" when the information is disclosed, other market participants could buy or sell ahead of the liquidity provider, making it more costly for the liquidity provider to hedge the transaction. If the liquidity provider anticipates such price movement, front-running by market participants could make the transaction more costly for the block trade initiator, as the liquidity provider may provide it with less favorable quotations in order to protect itself from the impact of such disclosure.[158] Some market participants also are concerned that if a block trade were required to interact with other trading interest on a SB SEF, there might not be enough liquidity on the SB SEF to execute the entire block trade, leaving a portion of the block trade unexecuted. These market participants are worried about the execution risk of doing block trades on a SB SEF. Not having a large trade filled, or having it filled at a disadvantageous price as a result of having to enter into more than one trade as part of the execution

[155] *See supra* note 152 for a description of a composite indicative quote.

[156] *See infra* Section VIII.D for a discussion of block trades.

[157] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(2)(C) of the Exchange Act).

[158] *See* Reporting and Dissemination Release, *supra* note 6, for a discussion of the concerns surrounding post-trade transparency.

process, could hurt investment performance.[159]

For these reasons, market participants have urged exceptions for the handling of block trades, including the ability to negotiate and execute block trades without having to interact with trading interest on the SB SEF. Market participants even have indicated a willingness to forego available pre-trade transparency in order to keep their proprietary block trading strategies private.

The Commission is sensitive to these concerns. However, the Commission also is concerned that allowing the execution of block trades on a SB SEF in a manner that is subject to less pre-trade transparency than the minimum level that would be required by Commission rules, for example, by allowing block trades to be executed off of the SB SEF and then reported to the SB SEF without interacting with trading interest on the SB SEF (*i.e.,* using the SB SEF as a "print facility"), could circumvent the mandatory trade execution requirement and undermine the goals of providing for more transparent and competitive trading on a SB SEF. Therefore, although the Commission believes that it is permissible for a SB SEF to establish different trading rules for block trades generally, block trades would still be subject to the various minimum requirements that the Commission has established with respect to pre-trade transparency[160] and interaction with other trading interest on the SB SEF, as discussed above.[161]

SB SEFs would have flexibility, therefore, to establish different rules for the trading of block trades on their facilities, as long as those rules were clear as to how block trades would be handled and would comply with the rules being proposed today.[162] A SB SEF could, for example, allow a limit order book platform to use a separate multi-dealer RFQ component to execute block trades, as long as the block trade interacts with existing interest on the SB SEF (*i.e.,* the limit order book portion of the SB SEF that handles orders that are not blocks) and otherwise complies with the proposed requirements that are part of this rulemaking. Also, under the Commission's proposed interpretation of the definition of SB SEF, a SB SEF that operates a RFQ platform and that requires an RFQ to be disseminated to all participants, could, for example, permit participants to choose to send an RFQ to fewer than all participants, including just one. In a system that allows participants to display firm quotes, the system (and rules) would need to be designed to provide that a block trade, like any other trade, would interact with the displayed orders based on a fair method. Thus, to the extent that liquidity exists on a central limit order book trading platform of the SB SEF, a block trade would be required to interact with those pre-existing resting bids and offers.[163] The Commission also notes that, until a SB swap that is determined to be subject to the mandatory clearing requirement and is determined to have been made "available to trade" on a SB SEF or an exchange, the SB swap could be traded in block size off a SB SEF or exchange.

The Commission is proposing to require that a SB SEF define a "block trade" to have the same meaning as in Rule 900 of Regulation SBSR relating to trade reporting.[164] This would mean that each SB SEF would use the same threshold for determining what constitutes a block trade for a particular "security-based swap instrument," as calculated by a registered SDR.[165] The Commission believes that it is important for each SB SEF to use the same threshold for block trades to ensure consistency and uniformity across SB SEFs.[166] The Commission notes, however, that until it establishes the criteria and formula for determining a block trade pursuant to proposed Rule 907(b) of Regulation SBSR, proposed Rule 800 of Regulation SB SEF would permit a SB SEF to set its own criteria and formula for determining what constitutes a block trade as long as such criteria and formula are consistent with the Core Principles and the rules and regulations thereunder.

The Commission seeks comments on its proposed definition and treatment of block trades. Should the definition of block trade have the same meaning in the context of a SB SEF and in the context of trade dissemination and reporting? Is there anything about pre-trade versus post-trade transparency that warrants having different definitions of a block trade in the context of proposed Regulation SB SEF and proposed Regulation SBSR? [167] Are there other definitions of block trade that the Commission should consider? Do commenters agree with the proposed approach to block trades on SB SEFs? Is pre-trade transparency for block trades desirable? If so, why? If not, why not? Should SB SEFs be permitted to have discretion regarding implementation of rules governing the handling of block trades? For example, should block trades be permitted to be executed in "one participant to one participant" transactions and then "printed" on the SB SEF? If the Commission were to adopt its proposed interpretation of the definition of SB SEF, would such flexibility be necessary in light of the fact that, under the proposed interpretation, a requester can choose to

[159] *See, e.g.,* Hendrik Bessembinder & Kumar Venkataraman, *Does an Electronic Stock Exchange Need an Upstairs Market?* J. of Fin. Econ., Vol. 73 (2004) ("Bessembinder Paper"), finding that execution costs of a block trade in an "upstairs" market are much lower than would be if the block trade were executed in a "downstairs" market.

[160] *See,* for example, *supra* Sections III.B and VIII.C, discussing the proposed requirement that SB SEFs that operate a RFQ mechanism disseminate a composite indicative quote and make it available to all participants, the aspects of the proposed interpretation that all responses to a request for quote be included within the composite indicative quote and that SB SEFs cannot limit the number of liquidity providers to whom a request for quote is sent.

[161] *See,* for example, *supra* Section VIII.C.

[162] Proposed Rule 811(d) would require that a SB SEF establish and enforce rules governing the procedures for trading on the SB SEF including the handling of block trades if different from other trades.

[163] If a SB SEF operated a central limit order book and a separate RFQ mechanism, the SB SEF's systems would be required to ensure that any trade to be executed in the RFQ mechanism interacted with any existing firm interest on the central limit order book at the same or better price before interacting with interest on the RFQ platform. For example, assume that such a SB SEF had a 5,000 notional resting order on its limit order book in SB swap A and that a 100,000 notional RFQ in SB swap A was entered into and disseminated to liquidity providers in the RFQ mechanism. If the resting limit order has a price equal to or greater than the price at which a response(s) comes back in the RFQ mechanism to execute the RFQ order, the SB SEF system would be required to execute 5,000 of the RFQ order against the resting limit order and 95,000 against the response(s).

[164] *See* proposed Rule 800 (defining "block trade" as having the same meaning as in Rule 900 of Regulation SBSR under the Exchange Act) and Reporting and Dissemination Release, *supra* note 6. Rule 900 of Regulation SBSR would define a block trade to mean a large notional SB swap transaction that meets the criteria set forth in Rule 907(b) of Regulation SBSR, which states that a registered SDR shall establish and maintain written policies and procedures for calculating and publicizing block trade thresholds for all security-based swap instruments reported to the registered SDR in accordance with the criteria and formula for determining block size as specified by the Commission.

[165] *See* Reporting and Dissemination Release, *supra* note 6, and proposed Rule 900 for a definition of "security-based swap instrument."

[166] The Commission notes that even if more than one registered SDR establishes the block trade threshold for a SB swap, the thresholds would be identical because each SDR in the same class of SB swap would use the same data to calculate the threshold. *See* Reporting and Dissemination Release, *supra* note 6, for a more detailed discussion.

[167] *See, e.g.,* Memorandum by the Staff of the Division of Risk, Strategy and Financial Innovation of the U.S. Securities and Exchange Commission to File No. S7–34–10, Release No. 34–63346, dated January 13, 2011. The memorandum is submitted as a comment letter to the Reporting and Dissemination Release, *supra* note 6, and is available at: *http://www.sec.gov/comments/s7-34-10/s73410-12.pdf.*

submit an RFQ fewer than all participants, including to just one participant? Should there be other exceptions for block trades, such as an exception for a clean cross? [168] What would be the benefits and drawbacks of such proposals? Should any such proposals be subject to any conditions, such as allowing block trades an exemption from the minimum pre-trade transparency and order interaction requirements on a temporary basis or not permitting "one participant to one participant" transactions to be printed on a SB SEF after trading activity in the SB swap crosses a specified liquidity threshold?

What would be the effect of requiring block trades to interact with existing interest on the SB SEF, to the extent firm trading interest is available? What impact, if any, would that requirement have on price competition occurring on the SB SEF in that particular SB swap? If hidden trading interest were permitted on a SB SEF's trading system, how should such interest be handled under the interaction requirement? If block trades were required to interact with hidden trading interest, would that encourage hidden interest and discourage displayed interest? What would be the impact of allowing block trades to be executed off of the SB SEF and then "printed" on a SB SEF, or to execute without interaction with existing interest? What impact, if any, would that have on price competition on the SB SEF in that particular SB swap? What impact would such a proposal have on the incentives of market participants to post firm interest in that SB swap? Would this proposal create a significant disincentive for market participants to enter any sizeable volume for execution on the SB SEF? What other requirements, if any, should the Commission impose to promote incentives to post firm quotes? Are there any alternative methods to provide for pre-trade transparency for block trades without requiring block trades to interact with other bids and offers on a SB SEF? If so, how would these alternative methods impact the requirements and goals of the Dodd-Frank Act? Are there alternative trading mechanisms, such as crossing systems, that could be used to trade blocks? How would these alternative trading mechanisms comply with the pre-trade transparency requirements? Are there other special provisions that should apply to block trades? If so, what are they, and why would they be appropriate?

The Commission recognizes that the SB swap market is different in certain respects than the market for cash equities and listed options. For example, many fewer market participants account for a significant amount of the trading in SB swaps. In addition, there is not at this time any direct retail participation in the SB swap market. Further, trading in SB swaps generally is much less liquid than for many NMS stocks and listed options. How, if at all, do these factors, or other factors regarding the structure of the SB swap market, impact the handling of block trades in the SB swap market, and how should they, if at all, impact the proposed treatment of block trades on SB SEFs?

E. Trade Processing Procedures

Proposed Rule 811(f) would require a SB SEF to establish and enforce rules concerning the reporting of trades executed on the SB SEF to a clearing agency and procedures for the processing of transactions in SB swaps that occur on or through the SB SEF, including, but not limited to, procedures to resolve any disputes concerning the execution of a trade.

The Commission believes that the types of rules contemplated by proposed Rule 811(f) are important to contributing to the fair and orderly functioning of any SB SEF, and to ensure that trades executed on a SB SEF are properly transmitted to the applicable registered clearing agency. In the Commission's view, these types of rules would aid a SB SEF in contributing to the operation of an orderly market. The Commission believes that the rules of the SROs could provide appropriate models to SB SEFs concerning the types of rules that would satisfy the requirements of this proposed rule. Alternatively, the Commission could find the rules of other regulated entities appropriate for use as models as well, upon review.

The Commission requests comment generally on all aspects of proposed Rule 811(f). Is the Commission's proposed rule sufficiently clear? Are there other aspects of trading procedures, aside from the reporting of trades to a clearing agency and procedures for the processing of transactions in SB swaps and for the handling of disputes that should be addressed? If so, what additional information should be included in such a rule? Should the Commission require SB SEFs to compare and report confirmed trades [169] to clearing agencies, or is it appropriate to leave the choice to SB SEFs? Please be specific.

F. Disciplinary Rules and Procedures

Proposed Rule 811(g) would require a SB SEF to establish rules and procedures concerning the disciplining of its participants including, but not limited to: authorizing the SB SEF's staff to recommend and take disciplinary action for alleged violations of the SB SEF's rules; specifying the sanctions that may be imposed on participants for violations of the SB SEF's rules (provided that each sanction is commensurate with the corresponding violation); and establishing fair and non-arbitrary procedures for any disciplinary process, and appeals thereof.

SB SEFs are required by Section 3D(d)(2) of the Exchange Act to enforce compliance with their rules. Proposed Rule 811(g) is designed to require the SB SEF to have baseline rules relating to its disciplinary process to help it carry out its statutory responsibilities.[170]

Proposed Rule 811(h) would require the SB SEF to make and keep specific records of all disciplinary proceedings and sanctions imposed, and all appeals, and to disclose disciplinary actions on an annual amendment to Form SB SEF and on the SB SEF's annual report of the CCO required by Section 3D(d)(14) of the Exchange Act and proposed Rule 823.[171] While this proposed requirement also would be part of the recordkeeping requirement of the SB SEF under Core Principle 9, the Commission is restating it in connection with Core Principle 2, since these records would need to be maintained and information about disciplinary actions disclosed by the SB SEF. This information, which could be used by the Commission to review the disciplinary process at a SB SEF, would provide the Commission with an additional tool to

[168] *See, e.g.,* National Stock Exchange Rule 11.12 describing acceptable clean cross orders as a cross: (1) That is for at least 5,000 shares and has an aggregate value of at least $100,000; (2) with a size greater than the size of the interest at each side of the top of book; and (3) with a price equal to or better than the Protected NBBO.

[169] This would parallel certain reporting requirements for locked-in trades in the equity and debt markets. A locked-in trade is one in which all of the terms and conditions of the trade are agreed to and accepted by the buyer and the seller. *See, e.g., http://www.amex.com/servlet/AmexFnDictionary?pageid=display&titleid=3784.*

[170] In fashioning their disciplinary rules, SB SEFs may be informed by the rules on disciplinary proceedings maintained by the national securities exchanges. *See, e.g.,* Chicago Board Options Exchange, Chapter XVII (Disciplinary Rules) and New York Stock Exchange Rules 475–477 (Disciplinary Rules).

[171] *See infra* Sections XXI (discussing Core Principle 14) and XXIII (discussing proposed Form SB SEF). The Commission notes that information provided on proposed Form SB SEF is public.

carry out its oversight responsibilities with respect to SB SEFs.[172]

The Commission requests comment generally on all aspects of proposed Rule 811(h). Is the Commission's rule concerning disciplinary rules and procedures sufficiently clear? Should the proposed rule include greater specificity regarding the disciplinary processes for SB SEFs, including the review of disciplinary actions? If so, what provisions should be included in any such rule? Should participants in the SB SEF, or customers of participants, be involved in the disciplinary process? If so, in what regard? Should the CCO be required to be involved in any disciplinary process?

G. Surveillance for Rule Violations

Proposed Rule 811(i) would require a SB SEF to establish rules and procedures to assure that the information to be used to determine whether rule violations have occurred is captured and retained in a timely manner. Proposed Rule 811(j) would require the SB SEF to have the capacity to capture information that may be used in establishing whether rule violations have occurred, including through the use of automated surveillance systems as set forth in proposed Rule 813(b),[173] maintain appropriate resources to fulfill these obligations, and investigate possible rule violations.

The Commission believes that, to be able to effectively carry out its obligations to enforce compliance with its rules, a SB SEF must have the capability to monitor trading activity to determine whether rule violations are occurring or have occurred.[174] The rules proposed in Rules 811(h) and (i) are designed to require a SB SEF to have baseline rules relating to surveillance of its market to help it carry out its statutory responsibilities.

The Commission requests comment generally on all aspects of proposed Rule 811(i). Are the Commission's proposed rules on surveillance of rule violations sufficiently clear? If not, what additional information is required? Please be specific. Should SB SEFs be required to exchange information with other SB SEFs that have listed the same SB swaps for trading to properly surveil trading in those SB swaps on its market? How would any exchange of information with other SB SEFs be accomplished? Should SB SEFs have access to trading information for similar SB swaps trading in the OTC derivatives market? If so, how would this be accomplished? What guidelines should the Commission use to determine what SB swaps are sufficiently similar to require such access? Should SB SEFs be required to share information with other regulatory authorities? For example, if a SB SEF detects unusually high activity in a particular SB swap, what guidelines would be appropriate for the sharing of this information with the Commission and other regulatory authorities that regulate the underlying asset?

IX. Core Principle 3—Manipulation

Section 3D(d)(3) of the Exchange Act (Core Principle 3) provides that a SB SEF shall permit trading only in SB swaps that are not readily susceptible to manipulation.[175] To implement Core Principle 3, the Commission is proposing Rule 812.

Proposed Rule 812(a) would implement the requirements of Core Principle 3. Proposed Rule 812(b) would provide that before a SB SEF may permit the trading of a SB swap on the SB SEF, the SB SEF's swap review committee must have determined, after taking into account all of the terms and conditions of the SB swap and the markets for the SB swap and any underlying security or securities, that such SB swap is not readily susceptible to manipulation. The proposed requirement that the swap review committee consider not only the market for the SB swap, but also the market for any underlying security or securities is intended to make clear that the swap review committee must consider whether an underlying or reference security could make a SB swap readily susceptible to manipulation.[176] Under proposed Rule 812(c), after a SB SEF commences trading of a SB swap, its swap review committee would be required to periodically review trading in the SB swap. If the swap review committee cannot determine, after taking into account all of the terms and conditions of the SB swap, the markets for the SB swap and any underlying security or securities, and trading in the SB swap, that such SB swap is not readily susceptible to manipulation, the SB SEF would be required to no longer permit the trading of the SB swap.

Because Core Principle 3 permits a SB SEF to trade only SB swaps that are not readily susceptible to manipulation, the Commission preliminarily believes that the proposal to require every SB SEF's swap review committee to consider the terms and conditions of the SB swap and the markets for the SB swap and any underlying security or securities, and make an affirmative determination that the SB swap is not readily susceptible to manipulation before a SB SEF trades a SB swap, and to periodically review that determination after trading commences, is a reasonable approach to implementing the statutory language of Core Principle 3. Further, as discussed above, proposed Rule 811(c)(1) would require a SB SEF's swap review committee to determine whether to trade a SB swap and whether a SB swap that has commenced trading should continue to trade on the SB SEF.[177] Under proposed Rule 812, the swap review committee would be required to also consider whether a SB swap raises manipulation concerns before trading such product.

The Commission generally requests comment on all aspects of proposed Rule 812. Additionally, the Commission requests comment as to whether there are any types of SB swaps trading today that a SB SEF's swap review committee should presume are not readily susceptible to manipulation. What factors would or should a SB SEF take into consideration when making a determination whether a SB swap would be readily susceptible to manipulation? Should the Commission provide more guidance regarding what being "readily susceptible to manipulation" means in the context of SB swaps? If so, what guidance should the Commission provide? Should the Commission require a SB SEF to consider objective criteria concerning

[172] *See* Regulation MC Proposing Release, *supra* note 82, 75 FR at 65912, discussing the requirement in proposed Rule 702(g) under Regulation MC relating to compositionally balanced disciplinary panels for SB SEFs.

[173] *See infra* Section X (discussing Core Principle 4). Core Principle 4, which would be implemented in proposed Rule 813, requires a SB SEF, among other things, to monitor trading in SB swaps to prevent manipulation, price distortion, and disruptions of the delivery or cash settlement process through surveillance, compliance, and disciplinary practices and procedures, including methods for conducting real-time monitoring of trading and comprehensive and accurate trade reconstructions.

[174] *See infra* Section X (discussing Core Principle 4).

[175] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(3) of the Exchange Act).

[176] The Commission notes that it is not unusual for national securities exchanges to include in their listing standards for derivatively-priced securities provisions concerning the market for the underlying components. *See, e.g.,* Chicago Board Option Exchange Rule 5.3 (listing standards for options contracts which include, among other things, requirements relating to the trading volume and number of holders of the underlying security); NYSE Arca Rule 5.2(j)(3) Commentary .01(a) (listing standards for index-based exchange-traded funds, which include, among other things, requirements relating to the trading volume and market value of underlying components).

[177] Pursuant to proposed Rule 811(c)(3), a SB SEF would be required to establish criteria that its swap review committee should consider in determining which SB swaps should trade on the SB SEF. *See supra* Section VIII.B.

the underlying security or securities? If so, what should these criteria be? [178]

The Commission recognizes that it might be difficult to determine whether a particular SB swap is readily susceptible to manipulation. Further, individual SB SEFs—as well as various market participants and investors—may have differing views on whether a particular SB swap is readily susceptible to manipulation. In light of the potential need for further clarity on this question, the Commission therefore requests comment on whether it should consider adopting a safe harbor consisting of objective criteria for purposes of meeting the requirements of Section 3D(d)(1) of the Exchange Act with respect to Core Principle 3. If so, what would be appropriate objective criteria for such a safe harbor provision? Should the criteria relate to characteristics of the SB swap or the market for the underlying, or the procedures to be followed by the SB SEF in making a determination as to whether an SB swap is readily susceptible to manipulation, or a combination of both? For example, should the Commission consider adopting a safe harbor that includes thresholds relating to trading volume, number of holders, and/or market value of the underlying security or securities? [179] Should the criteria to be included in any safe harbor be the same as or different from any criteria that the Commission may adopt with respect to the mandatory clearing determination or the determination of when a SB swap is made available to trade? Commenters are requested to be as specific as possible as to what the appropriate criteria for a safe harbor would be.

Is the proposed periodic review requirement necessary or appropriate? Should the Commission define how frequently a SB SEF must review its determination that a SB swap is not readily susceptible to manipulation? If so, what would be an appropriate frequency for such a review?

X. Core Principle 4—Monitoring of Trading and Trade Processing

Section 3D(d)(4) of the Exchange Act (Core Principle 4) requires a SB SEF to establish and enforce rules or terms and conditions defining or specifications detailing: (i) trading procedures to be used in entering and executing orders traded on or through the facilities of the SB SEF; and (ii) procedures for trade processing of SB swaps on or through the facilities of the SB SEF.[180] This Core Principle also requires SB SEFs to monitor trading in SB swaps to prevent manipulation, price distortion, and disruptions of the delivery or cash settlement process through surveillance, compliance and disciplinary practices and procedures, including methods for conducting real-time monitoring of trading and comprehensive and accurate trade reconstructions.[181] The Commission is proposing Rule 813 of Regulation SB SEF to implement Core Principle 4. The Commission believes that the requirements of proposed Rule 813 would aid potential registrants in evaluating whether the rules they propose to implement and the mechanisms they would establish to monitor trading in SB swaps would comply with the Core Principle.

Proposed Rule 813(a) would implement the statutory language of the Core Principle. Proposed Rule 813(b) would require a SB SEF to have the capacity and appropriate resources to electronically monitor trading in SB swaps on its market by establishing an automated surveillance system, including real time monitoring of trading and the use of automated alerts, that is designed to detect and deter any fraudulent or manipulative acts or practices, including insider trading or other unlawful conduct or any violations of the rules of the SB SEF; to detect and deter market distortions or disruptions of trading that may impact the entry and execution of trading interest or the processing of trading interests; to conduct real-time monitoring of trading to provide for comprehensive and accurate trade reconstruction; and to collect and assess data to allow the SB SEF to respond promptly to market abuses or disruptions. The Commission preliminarily believes that requiring a SB SEF to establish such an automated surveillance system would enable the SB SEF to comply with the requirements of Core Principle 4 that SB SEFs monitor trading in SB swaps to prevent price manipulation, price distortion, and disruptions of the delivery or cash settlement process. In addition, Core Principle 4 specifically requires SB SEFs to have methods for conducting real-time monitoring of trading.[182]

Proposed Rule 813(c) would require a SB SEF to establish and enforce rules that require any participant that enters an order, request for quote, or other trading interests, or executes any transaction on the SB SEF to maintain books and records of any such order, request for quote or other trading interests, or transaction, and any positions in any SB swap that is the result of any such order, request for quote, or other trading interest or transaction on the SB SEF, and to provide prompt access to such books and records to the SB SEF and the Commission. Finally, proposed Rule 813(d) would require a SB SEF to establish and maintain procedures to investigate possible rule violations, to prepare reports of the findings and recommendations of such investigations, and to take corrective actions, as necessary.

The proposed rule's requirement that participants maintain books and records of their activity on the SB SEF and make them available to the SB SEF and the Commission would aid the SB SEF in detecting and deterring fraudulent and manipulative acts with respect to trading on its market, as well as help it to fulfill the statutory requirement in Core Principle 4 that a SB SEF monitor trading in SB swaps, including through comprehensive and accurate trade reconstructions. The proposed rule also would aid the Commission in carrying out its responsibility to oversee the SB SEF. The proposed rule's requirement that the SB SEF establish and enforce procedures to investigate possible rule violations and prepare reports is designed to ensure that the SB SEF fulfills its statutory obligation under this Core Principle to prevent manipulation, price distortions, and disruptions in the market.

The Commission requests comment on all aspects of proposed Rule 813. Is the proposed rule sufficiently clear? Do commenters believe that SB SEFs would encounter issues in establishing an automated surveillance system for real-time monitoring of trading and in collecting or assessing data to allow the SB SEF to respond promptly to market abuses or disruptions? Would proposed Rule 813(c), which would require participants to provide access to their books and records to the SB SEF and the Commission, be difficult for any particular group of participants (*e.g.,* non-registered ECPs or foreign participants) to comply with? If so, how should the Commission modify the rule to address any such issues?

Should SB SEFs be required to exchange information with each other regarding trading by their mutual participants to facilitate surveillance and investigation of potential

[178] *See supra* note 176, noting examples of national securities exchanges that have included in their listing standards for derivatively-priced securities required consideration of factors such as the trading volume, number of holders, and market value of the underlying security or securities.

[179] *See supra* note 176.

[180] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(4) of the Exchange Act).

[181] *Id.*

[182] *Id.*

manipulative or otherwise violative activity? If so, under what circumstances? Should SB SEFs be required to become members of the Intermarket Surveillance Group ("ISG"),[183] or to form a similar group among themselves? If so, should all SB SEFs be required to join? If not, what types of SB SEFs should be required to join? For example, should SB SEFs be required to join if they trade a certain volume threshold of SB swaps? If so, what should that volume threshold be? Should SB SEFs be required to share information with other regulatory authorities (including SROs)? For example, if a SB SEF detects an unusually high activity in a particular SB swap, what guidelines would be appropriate for the sharing of this information with the Commission and the other regulatory authorities that regulate the underlying asset?

XI. Core Principle 5—Ability To Obtain Information

Section 3D(d)(5) of the Exchange Act (Core Principle 5) requires a SB SEF to establish and enforce rules that would allow the SB SEF to obtain any necessary information to perform any of the functions described in the Core Principles for SB SEFs, provide the information to the Commission on request, and have the capacity to carry out such international information-sharing agreements as the Commission may require.[184] To implement Core Principle 5, the Commission is proposing Rule 814 of Regulation SB SEF.

Proposed Rule 814(a) would require each SB SEF to establish and enforce rules requiring its participants to furnish to the SB SEF, upon request and in the form and manner prescribed by the SB SEF, any information that is necessary for the SB SEF to perform its responsibilities including, without limitation, surveillance, investigating, examinations and discipline of participants. Such information may include, without limitation, financial information, books, accounts, records, files, memoranda, correspondence, and any other information pertaining to orders, requests for quotes, responses, quotations, or other trading interest entered and transactions executed on or through the SB SEF.[185] Proposed Rule 814(a) further would require each SB SEF to establish and enforce rules requiring its participants to cooperate with the SB SEF and any representative of the Commission and allow access by the SB SEF and any representative of the Commission at such reasonable times as the SB SEF or the Commission representative may request to examine the books and records of the SB SEF participant, or to obtain or verify other information related to orders, requests for a quote, responses, quotations, or other trading interest entered and transactions executed on or through, the SB SEF's facilities. These provisions would permit a SB SEF and any representative of the Commission to have access to any information that the SB SEF participants are required to make, keep, and preserve pursuant to any Commission or other rule, and should therefore assist the SB SEF to more effectively perform its obligations, as required by the Core Principles, and the Commission to perform its oversight responsibilities for SB SEFs.

Proposed Rule 814(b) would similarly require the SB SEF to cooperate with any representative of the Commission and allow access by any representative of the Commission to examine the books and records required to be kept by the SB SEF pursuant to proposed Rule 818, to obtain or verify other information related to orders, requests for quote, responses, quotations, or other trading interest entered and transactions executed on or through its facilities, and otherwise provide to any representative of the Commission, upon request, such information that the SB SEF may possess or obtain from its participants pursuant to proposed Rule 814(a). The Commission preliminarily believes that these provisions would be instrumental in enabling the Commission to carry out its oversight and regulation of SB SEFs and the SB swap market and would support the requirement in Core Principle 5 that the SB SEF establish and enforce rules that would allow the SB SEF to obtain any necessary information to perform any of the functions described in the Core Principles and provide the information to the Commission on request.

The Commission preliminarily believes that proposed Rule 814 would reasonably clarify the statutory language of Core Principle 5, which requires a SB SEF to have the ability to "obtain information" and "provide the information to the Commission on request." Specifically, the Commission believes that it is important to its ability to regulate and oversee SB SEFs for the Commission to be able to obtain information by specifying that SB SEFs and SB SEF participants must cooperate, furnish information upon request, provide access to books and records, and be subject to examination.[186] These proposed requirements also would enable the SB SEF to monitor participants on its system and enforce compliance with its rules, as required by Section 3D(d) of the Exchange Act.

Further, proposed Rule 814(b)(3) would require a SB SEF to have the capacity to carry out such international information-sharing agreements as the Commission may require.[187] Proposed Rule 814(b)(4) would require every SF SEF to certify at the time of registration on Form SB SEF, and annually thereafter as part of the annual compliance report described in Rule 823, that the SB SEF has the capacity to fulfill its obligations under any international information-sharing agreements to which it is a party as of the date of such certification.

These proposed regulations would implement the provision of Core Principle 5 requiring SB SEFs to have the capacity to carry out such

[183] ISG was established in the early 1980s and is comprised of an international group of exchanges, market centers and market regulators. ISG states that its purpose is to effectively detect and prevent unfair transactions across markets through market information sharing among its members. *See* ISG's Web site at *http://www.isgportal.org* for additional information on ISG.

[184] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(5) of the Exchange Act).

[185] The requirement that SB SEF participants make, keep and preserve books and records is independent of proposed Rule 814. *See* 17 CFR 240.17a–3 and 240.17a–4, which are applicable to registered broker-dealers. *See also* Public Law 111–203, § 764(a) (adding Section 15F(f)(B) of the Exchange Act, requiring each registered SB swap dealer and major SB swap participant to keep books and records as may be prescribed by the Commission). *See also* proposed Rule 809(c)(2)(i), requiring registered SB swap dealers and registered major SB swap participants to meet the minimum recordkeeping and reporting requirements imposed by the Commission. With respect to eligible contract participants, proposed Rule 809(c)(2)(ii) would require eligible contract participants to meet the recordkeeping and reporting requirements established by the SB SEF pursuant to proposed Rule 813.

[186] The proposed requirements are analogous to the provisions of Section 17(b) of the Exchange Act, which provides that the records of a national securities exchange, among other things, shall be subject to reasonable periodic, special or other examinations by representatives of the Commission, and Rule 17a–4(j) under the Exchange Act, requiring exchange members, brokers and dealers to furnish promptly copies of records that are required to be preserved under the rule to representatives of the Commission. 15 U.S.C. 78q(b)(1) and 17 CFR 240.17a–4(j).

[187] The Commission notes that it is not unusual for a national securities exchange to enter into an information-sharing agreement with a foreign exchange for the purpose of securing information in connection with trading in securities on the foreign exchange that could impact the trading of securities on the U.S. exchange. *See, e.g.,* Securities Exchange Act Release No. 59835 (April 28, 2009), 74 FR 21041 (May 6, 2009) (noting, in connection with proposed listing standards, that NYSE Arca, Inc. had in place an information sharing agreement with the London Metal Exchange ("LME") for the purpose of providing information in connection with trading in or related to futures contracts traded on LME.

international information-sharing agreements as the Commission may require. The Commission preliminarily believes that the proposed rule would help ensure that the SB SEF has the ability to fulfill its regulatory and reporting responsibilities with respect to its market place and its participants, and that the Commission has the information necessary to fulfill its oversight and regulatory responsibilities related to the SB swaps market. The proposed rule also would facilitate information-sharing in the global SB swaps market.

The Commission requests comment on all aspects of proposed Rule 814 relating to the ability to obtain information. Is the proposal that a SB SEF require its participants to furnish information upon request, cooperate with and provide access to the SB SEF too burdensome? Is the proposal that the SB SEF require its participants to furnish information upon request, cooperate with and provide access to any representative of the Commission appropriate?

Is the proposal to similarly require the SB SEF to furnish information upon request, cooperate with and provide access to any representative of the Commission at reasonable times as requested, appropriate? Are there other approaches that the Commission should take to implement the requirement that the SB SEF have the ability to obtain information and provide it to the Commission? Is there information that SB SEFs should be required to provide to the Commission on a regular, periodic basis? If so, what types of information should be provided in such a manner? How often should such information be provided?

Are there any other requirements with respect to international information-sharing agreements that a SB SEF should be required to comply with? Are the proposed requirements too burdensome? If so, why? What are the costs and benefits of the proposed requirements? Should the Commission require a SB SEF to enter into information-sharing agreements with U.S. trading venues for SB swaps, as the Commission may require, or as necessary or appropriate to fulfill its regulatory and reporting responsibilities? Are there any other requirements with respect to domestic information-sharing agreements with which a SB SEF should be required to comply? If so, please explain.

XII. Core Principle 6—Financial Integrity of Transactions

Section 3D(d)(6) of the Exchange Act (Core Principle 6) requires every SB SEF to establish and enforce rules and procedures for ensuring the financial integrity of SB swaps entered on or through the facilities of the SB SEF, including the clearance and settlement of SB swaps pursuant to Section 3C(a)(1) of the Exchange Act.[188] Pursuant to Section 3C(a)(1) of the Exchange Act, SB swap transactions must be cleared through a clearing agency registered with the Commission or a clearing agency exempt from registration, if the Commission has determined that the SB swap is required to be cleared.[189]

The Commission believes that it is important that SB SEFs set specific standards designed to ensure the financial integrity of all their participants. Proposed Rule 815(a) would implement the requirements of Section 3D(d)(6) of the Exchange Act. Proposed Rule 815(b) would permit the rules of a SB SEF to allow a participant trading a SB swap that will not be cleared through a registered clearing agency to consider counterparty credit risk in selecting potential counterparties, notwithstanding the requirements of proposed Rule 810(b)(2).[190] The Commission believes that these requirements, taken together, should strengthen the financial integrity of SB swap transactions that occur on the SB SEFs by reducing the counterparty credit risks associated with uncleared SB swaps transactions.

As noted above,[191] the Commission identified in the Regulation MC Proposing Release certain conflicts of interest that may provide incentives for certain dominant market participants to limit access by potential competing market participants to SB SEFs. A SB SEF could put in place participant standards, including capital requirements and other financial requirements, in a way that would unfairly restrict access to a SB SEF. For example, a SB SEF could have a very high capital requirement for participation that may exclude some smaller dealers from participation in the SB SEF. On the one hand, while appropriate participation standards, including financial requirements, would support this Core Principle that requires SB SEFs to have rules and procedures for ensuring the financial integrity of SB swaps entered on or through the facilities of the SB SEF, unduly high standards may without justification exclude persons who are otherwise qualified to trade on the SB SEF. On the other hand, the Commission is mindful that broadening access could come at the expense of sound risk management practices. Thus, lessening capital or other financial requirements to increase participation beyond a certain level may increase the overall risk of the SB SEF's operations.

The Commission seeks comments on all aspects of this proposed Rule 815. The Commission seeks comments on whether an SB SEF should be prohibited from imposing higher capital requirements than the capital requirements imposed by any rules or regulations that the Commission may impose on participants of SB SEFs because such higher standards could be utilized as a means to deter access to a SB SEF. If such a prohibition were adopted, would it be appropriate for the SB SEF to tailor capital requirements to the status of the participant on an objective basis, *e.g.,* having different capital requirements for a liquidity provider with market maker obligations than a participant without such obligations? If adopted, should such prohibition apply to trading in cleared and uncleared SB swaps? In addition, the Commission seeks comment on what additional safeguards, if any, would be necessary to ensure the financial integrity of SB swap transactions executed on a SB SEF. For swaps cleared by a registered clearing agency, should a SB SEF be required to ensure that it has the capacity to route transactions to the clearing agency? With respect to swaps that are not cleared, should a SB SEF be required to have rules requiring the transacting members to have entered into a credit arrangement for the transaction, demonstrate an ability to exchange collateral, and have appropriate credit filters in place?

XIII. Core Principle 7—Emergency Authority

Section 3D(d)(7) of the Exchange Act (Core Principle 7) requires SB SEFs to adopt rules to provide for the exercise

[188] *See* Public Law 111–203, § 763(a) (adding Section 3C(a)(1) of the Exchange Act).

[189] The clearing requirement in Section 3C(a) of the Exchange Act contains certain exceptions. For example, Section 3C(g) of the Exchange Act states that a counterparty that is not a financial entity that is using a SB swap to hedge or mitigate commercial risk is not subject to the clearing requirement. Section 3C(g)(1)(C) requires each such counterparty to notify the Commission of how it generally meets its financial obligations associated with entering into non-cleared SB swaps. *See* Section 3C of the Exchange Act for all applicable exceptions and exemptions to the clearing requirements for SB swaps and the requirements relating to clearing agencies of SB swaps.

[190] Proposed Rule 810(b)(2) would prohibit a SB SEF's rules from unreasonably limiting any person in respect to access to the services offered by such SB SEF in an unfair or discriminatory manner. *See supra* Section VII for a discussion of proposed Rule 810(b)(2).

[191] *See supra* Section VI, discussing access to SB SEFs.

of emergency authority, in consultation or cooperation with the Commission, as is necessary and appropriate, including the authority to liquidate or transfer open positions in any SB swap or to suspend or curtail trading in a SB swap.[192] The Commission is proposing Rule 816 to implement Core Principle 7.

Proposed Rule 816(a) would require that every SB SEF establish rules and procedures to provide for the exercise of emergency authority, in consultation or cooperation with the Commission, as necessary or appropriate. "Emergency" would be defined in proposed Rule 800 to have the same meaning as set forth in Section 12(k)(7) of the Exchange Act.[193] The Commission believes that the definition of "emergency" in Section 12(k)(7) of the Exchange Act has the advantage of being broad enough to cover unusual or extreme circumstances without being unduly restrictive. The Commission also believes that the proposed use of the Exchange Act's definition of emergency would foster consistency among rules regarding the exercise of emergency authority and promote the use of a consistent definition across securities markets generally.

Proposed Rule 816(c) would require that every SB SEF have rules that permit the SB SEF to immediately take any or all of the following actions during an emergency: (1) Impose or modify trading limits, price limits, position limits, or other market restrictions, including suspending or curtailing trading on its market in any SB swap or class of SB swaps; (2) extend or shorten trading hours; (3) coordinate trading halts with markets trading a security or securities underlying any SB swap; (4) coordinate with a registered clearing agency to liquidate or transfer positions in any open SB swap of one of its participants; and (5) any action directed by the Commission. The Commission preliminarily believes that the actions proposed in proposed Rule 816(c)(1) through (4) would be important powers for a SB SEF to have immediately without the need to seek additional authority from the Commission when an emergency has occurred. The proposed rule would enable a SB SEF to respond promptly during an emergency to maintain fair and orderly markets and foster market integrity and efficiency when ordinary authority would be insufficient.

In light of the breadth of the proposed emergency authority for SB SEFs, proposed Rule 816 also would require that every SB SEF have rules governing the exercise of such emergency authority. Pursuant to proposed Rule 816(b), SB SEF rules and procedures would be required to specify: the person or persons authorized by the SB SEF to declare an emergency; how the SB SEF would notify the Commission and the public of its decision to exercise its emergency authority; the processes for decision making by facility personnel with respect to exercise of emergency authority, including alternate lines of communication and guidelines to avoid conflicts of interest in the exercise of such authority; and the processes for determining that an emergency no longer exists and notifying the Commission and the public of such decision. The Commission believes that it is important that SB SEFs put in place a process for exercising emergency authority in order to help ensure that a SB SEF is prepared prior to any emergency situation and to help ensure that a SB SEF exercises emergency authority appropriately and uniformly.

Proposed Rule 816(d) would require every SB SEF to promptly notify the Commission of the exercise of its emergency authority and, within two weeks following cessation of the emergency, submit written documentation explaining the basis for declaring an emergency, how conflicts of interest were minimized, and the extent to which the facility considered the effect of its emergency action on the markets for the SB swap and any security or securities underlying the SB swap. Proposed Rule 816(d) also would provide that, if a SB SEF implements any rule or rule amendment in the exercise of its emergency authority, it shall file such rule or rule amendment with the Commission pursuant to Rule 806 prior to the implementation of such rule or rule amendment, or, if not practicable, within 24 hours after implementation of such rule or rule amendment. The Commission preliminarily believes that while it is important to provide SB SEFs with the tools necessary to react in emergency situations, requiring SB SEFs to submit a notice and, if applicable, file a certified emergency rule or rule amendment in accordance with proposed Rule 806, would help to deter SB SEFs from using such tools inappropriately. In addition, requiring a SB SEF to notify the Commission and, if applicable, file a certified emergency rule or rule amendment, would allow the Commission to determine whether a SB SEF acted in compliance with proposed Rule 816 and should provide the Commission timely information with respect to the actions taken in any emergency situation.

While some national securities exchanges have rules providing for the exercise of emergency authority by the exchange,[194] there is no specific Commission rule detailing how national securities exchanges should address the issue of emergency authority. In light of the mandate in Core Principle 7 that SB SEFs adopt rules governing the exercise of emergency authority, and in light of the fact that it is likely the same entities will be registered as SB SEFs and SEFs, the Commission's approach to implementing Core Principle 7 is guided by the approach the CFTC has taken with respect to the CEA's requirement that a designated contract market adopt rules to provide for the exercise of emergency authority.[195]

The Commission generally requests comment on all aspects of the proposed rule regarding emergency authority. Additionally, the Commission requests comments as to whether the proposed list of emergency actions that a SB SEF may take is appropriate. Are there any additional actions that should be included? Are there any proposed actions that should not be included? Why or why not?

The Commission notes that it is common for a national securities exchange to consult and cooperate with the Commission prior to responding to highly unusual or emergency market

[192] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(7) of the Exchange Act).

[193] *See* 15 U.S.C. 78*l*(k)(7) (defining the term emergency to mean "(A) a major market disturbance characterized by or constituting—(i) sudden and excessive fluctuations of securities prices generally, or a substantial threat thereof, that threaten fair and orderly markets; or (ii) a substantial disruption of the safe or efficient operation of the national system for clearance and settlement of transactions in securities, or a substantial threat thereof; or (B) a major disturbance that substantially disrupts, or threatens to substantially disrupt—(i) the functioning of securities markets, investment companies, or any other significant portion or segment of the securities markets; or (ii) the transmission or processing of securities transactions."

[194] *See, e.g.,* NYSE Rule 49 and Nasdaq Bylaws Article IX, Section 5.

[195] *See* Section 5(d) of the CEA, 7 U.S.C. 7(d) (requiring a board of trade to adopt rules to provide for the exercise of emergency authority, in consultation or cooperation with the CFTC, where necessary and appropriate). *See also* 17 CFR part 38, Appendix B to part 38 implementing Section 5(d) of the CEA. Appendix B to part 38 provides, in part, that a designated contract market should have clear procedures for the exercise of emergency authority and should, among other things, be able to impose or modify price limits, order the liquidation or transfer of open positions, order the fixing of a settlement price, order a reduction in positions, extend or shorten the expiration date or the trading hours, suspend or curtail trading on the market, order the transfer of customer contracts and the margin for such contracts from one member including non-intermediated market participants of the contract market to another, or alter the delivery terms or conditions, or, if applicable, should provide for such actions through its agreements with its third-party provider of clearing services.

conditions and expects that a SB SEF would likely do the same before exercising its emergency authority pursuant to proposed Rule 816. However, the Commission requests comment on whether it should require that a SB SEF consult and cooperate with the Commission before it takes any emergency action. Why or why not? Is the proposed definition of emergency appropriate? Is there another definition of emergency that would be more appropriate? Would it be preferable for the Commission not to define the term emergency? If not, why not? The Commission further requests comment on whether the proposed list of rules specifying processes for exercising emergency authority in proposed Rule 816(b) is appropriate. Are there any additional processes that should be included? Are there any proposed processes that should not be included? Why or why not?

XIV. Core Principle 8—Timely Publication of Trading Information

Section 3D(d)(8) of the Exchange Act (Core Principle 8) requires SB SEFs to make public timely information on price, trading volume, and other trading data on SB swaps to the extent prescribed by the Commission and to have the capacity to electronically capture and transmit and disseminate trade information with respect to transactions executed on or through the facility.[196] Section 13(m)(1) of the Exchange Act separately authorizes the Commission to make SB swap transaction, volume and pricing data available to the public in such form and at such times as the Commission determines appropriate to enhance price discovery.[197] The Commission has separately proposed rules relating to the reporting and public dissemination of SB swap transaction and pricing data.[198]

To implement Core Principle 8, the Commission is proposing Rule 817. Proposed Rule 817(a) enumerates the requirements of Section 3D(d)(8) of the Exchange Act. Thus, every SB SEF would be required to: (1) Have the capacity to electronically capture, transmit, and disseminate information on price, trading volume, and other trading data on all SB swaps executed on or through the SB SEF; and (2) make public timely information on price, trading volume, and other trading data on SB swaps, to the extent and in the manner prescribed by the Commission. As noted, the Commission has separately proposed rules relating to the public dissemination of SB swap transaction and pricing data.[199] The Commission is not at this time proposing any additional requirements on SB SEFs relating to the public dissemination of such data.[200]

In addition, proposed Rule 817(b) would require that, if any SB SEF makes available information regarding a SB swap transaction to any person other than a counterparty to the transaction, then the SB SEF must make that information available to all participants on terms and conditions that are fair and reasonable and not unfairly discriminatory. This proposed requirement is designed to prevent a SB SEF from providing information on SB swap transactions to certain persons (other than counterparties) and not to others, or provide such information pursuant to different terms that are not justified. The Commission believes that fair, reasonable, non-discriminatory access to market information is essential to providing a level playing field for all market participants and that the proposed requirement in Rule 817(b) would prevent developments in the SB swap market that could undermine the goal of post-trade price transparency.

Proposed Rule 817(c) would also prohibit a SB SEF from making any information regarding a SB swap transaction publicly available prior to the time a SDR is permitted to do so under proposed Rule 902 of Regulation SBSR under the Act.[201]

The Commission understands, however, that for business reasons counterparties to a SB swap transaction may prefer to have a SB SEF act as its reporting agent for purposes of complying with the counterparty's responsibility under proposed Regulation SBSR to report required transaction information to a registered SDR. Proposed Rule 817(b) therefore would permit a SB SEF, acting as agent, to report transaction information on behalf of a counterparty responsible for submitting transaction information to a registered SDR. Under proposed Rule 817(c), SB SEFs would be permitted to publicly disseminate SB swap transaction information, but could not do so prior to the time SDRs would be permitted to do so under proposed Rule 902 of Regulation SBSR under the Act. Thus, a SB SEF could not publicly disseminate complete transaction reports for block trades (*i.e.,* including the transaction ID and the full notional size) until the times specified in Rule 902(b)(1) through (3).[202]

The Commission believes that its proposed rules for implementation of Core Principle 8 would clarify the extent and manner in which SB SEFs could make information on transactions executed on the SB SEF available in a manner consistent with the requirements of proposed Regulation SBSR. The Commission requests comment on all aspects of proposed Rule 817 with respect to the timely publication of trading information. Additionally, the Commission requests comment on whether the proposed role of SB SEFs in the public dissemination of transaction information is appropriate. Should SB SEF's be able to compete with SDRs for potential customers of transaction data? How, if at all, would the prohibition on dissemination of transaction information in proposed Rule 902 of Regulation SBSR impact the development of the market for SB swaps? Should the Commission prohibit

[196] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(8) of the Exchange Act).

[197] *See* Public Law 111–203, § 763(i), (adding Section 13(m) of the Exchange Act).

[198] The Commission recently proposed Regulation SBSR that would require reporting and real-time public dissemination of certain information regarding SB swap transactions. Proposed Regulation SBSR identifies the SB swap information that would be required to be reported and disseminated, establishes reporting obligations, and specifies the time frames for reporting and disseminating. Proposed Regulation SBSR would require a registered SDR to publicly disseminate certain SB swap information that is reported to it in real time. *See* Reporting and Dissemination Release, *supra* note 6.

[199] *Id.*

[200] The rules proposed by the Commission pursuant to Section 13(m) of the Exchange Act would limit the public dissemination of SB swap transaction information by any person other than a registered SDR. Specifically, proposed Rule 242.902(d) of Regulation SBSR would prohibit any person other than a registered SDR from making available to one or more persons (other than a counterparty) information relating to a SB swap before the earlier of: (1) 15 minutes after the time of execution of the SB swap; or (2) the time that a registered SDR publicly disseminates a report of that SB swap. This prohibition on dissemination to one or more persons (other than a counterparty) during such time period would apply to SB SEFs and its participants, as it would to all other persons. *See* Reporting and Dissemination Release *supra* note 6.

[201] The Commission recently proposed Regulation SBSR, which would require reporting and real-time public dissemination of certain information regarding SB swap transactions. Proposed Regulation SBSR identifies the SB swap information that would be required to be reported and disseminated, establishes reporting obligations, and specifies the timeframes for reporting and disseminating. Proposed Regulation SBSR would require a registered SDR to publicly disseminate certain SB swap information that is reported to it in real time. *See* Reporting and Dissemination Release *supra* note 6.

[202] As proposed, subject to some exceptions, Rule 902(b) of Regulation SBSR would prohibit the public dissemination of the complete transaction report of a block trade (including the transaction ID and the full notional size): (1) Executed on or after 5:00 UTC and before 23:00 UTC of the same day, until 7:00 UTC of the following; and (2) executed on or after 23:00 UTC and up to 5:00 UTC of the following day, until 13:00 UTC of that following day.

a SB SEF from disseminating the full size of a block trade after the period specified in Rule 902(d), which could be after 15 minutes, but before a SDR has disseminated the full size of the block trade? Would such a prohibition be necessary? Or is it reasonable to expect that a SB SEF would not disseminate block trade information before a SDR if the SB SEF's market participants did not want dissemination of such information? With respect to data that a SDR is required to disseminate under proposed Rule 902 of Regulation SBSR, would proposed Rule 817(c) be effective in ensuring that SB SEF data feeds do not have any advantage over SDR data feeds? If not, should the proposed rule be revised, and if so, how so? Are SB SEFs likely to sell or otherwise disseminate market data following dissemination of data by a registered SDR? If not, why not?

XV. Core Principle 9—Recordkeeping

Section 3D(d)(9) of the Exchange Act (Core Principle 9) requires SB SEFs to 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. This Core Principle also requires SB SEFs to report to the Commission, in a form and manner acceptable to the Commission, such information as the Commission determines to be necessary or appropriate for the Commission to perform the duties of the Commission under the Exchange Act. In addition, this Core Principle requires the Commission to adopt data collection and reporting requirements for SB SEFs that are comparable to corresponding requirements for clearing agencies and SDRs.

The Commission is proposing Rule 818 setting forth the recordkeeping and reporting obligations of SB SEFs to implement this Core Principle. This proposed rule is comparable to the recordkeeping and reporting obligations of national securities exchanges and ATSs under the Exchange Act.[203]

Proposed Rule 818(a) would require every SB SEF to keep and preserve at least one copy of all documents, including all correspondence, memoranda, papers, books, notices, accounts, and other such records, including the audit trail records, as shall be made and received in the conduct of its business. Proposed Rule 818(b) would require SB SEFs to keep and preserve such documents and other records for a period of not less than five years, the first two years in an easily accessible place. Proposed Rule 818(c) would require SB SEFs to establish and maintain the records necessary to create a meaningful audit trail. Specifically, the Commission proposes that SB SEFs establish and maintain accurate, time-sequenced records of all inquiries, responses, orders, quotations or other trading interest, and transactions that are received by, originated on, or executed on the SB SEF.[204] These records must include the key terms of each inquiry, response, order, quotation or other trading interest or transaction and must document the complete life of each inquiry, response, order, quotation or other trading interest or transaction on the SB SEF, including any modification, cancellation, execution, or any other action taken with respect to such order, inquiry, response, quotation, or transaction.[205] Further, proposed Rules 818(e) and (f) would require a SB SEF to report to the Commission such information as the Commission may, from time to time, determine to be necessary for the Commission to perform its duties under the Exchange Act, and upon request of any representative of the Commission, to promptly furnish to each representative copies of any documents, in such form and manner acceptable to such representative, required to be kept and preserved by the SB SEF pursuant to proposed Rules 818(a) and (b).

The Commission would use the information required under proposed Rules 818(a) through (c) to carry out its oversight responsibility over SB SEFs. The records required to be kept, maintained, and provided to the Commission under these provisions would provide an additional tool to help the Commission to determine whether a SB SEF is operating in compliance with the Exchange Act and the rules and regulations thereunder. The audit trail information required to be maintained under proposed Rule 818(c) would facilitate the ability of the SB SEF and the Commission to examine the complete history of all trading interest entered into and transactions executed on a SB SEF. This audit trail information would help the SB SEF and the Commission to detect and deter fraudulent and manipulative acts and prepare reconstructions of activity on a SB SEF or in the SB swaps market, and generally to understand the causes of unusual market activity.

Proposed Rule 818(d) would require a SB SEF to establish, maintain, and enforce written policies and procedures to verify the accuracy of the transaction data it collects and reports.[206] This requirement is based on the premise that transaction data is only useful if it is accurate. If it is not accurate, then it will not enhance transparency. The SB swaps market participants must be able to trust that the information they receive is accurate in order to make appropriate investment decisions. Further, a SB SEF must have accurate information if it is to effectively carry out its obligations to surveil the market and enforce it rules. Similarly, the Commission must be able to trust that the information it receives is accurate so that it can oversee the market and properly determine whether the SB SEF is carrying out its statutory mandate.

The Commission requests comment on all aspects of proposed Rule 818. Are the documents required to be preserved pursuant to proposed Rule 818(a) appropriate? Are there additional documents that a SB SEF should be required to preserve? Is the proposed time period for record retention appropriate? Should SB SEF's be required to keep such records for a longer or shorter period of time? Are the records required to be preserved to maintain an audit trail pursuant to proposed Rule 818(c) appropriate? Are there additional records that a SB SEF should be required to keep? Should the Commission require SB SEFs to keep audit trail records in a particular format? What are the benefits and drawbacks of allowing each SB SEF to determine its own format to keep audit trail records? Would allowing each SB SEF to determine its own format for the maintenance of an audit trail hamper the Commission's ability to analyze trading activity across multiple SB SEFs? If yes, then how?

Is it appropriate to require SB SEFs to have policies and procedures to verify the accuracy of transaction data? If not, why not? In the absence of such requirements, how should the Commission ensure the integrity of transaction data that originates on or passes through a SB SEF? What are the specific benefits and drawbacks of any suggested approaches?

Proposed Rules 818(e) and (f) require a SB SEF to promptly furnish information and records required to be kept under the Rule to the Commission upon request. What, if any, additional reports or records should be furnished to the Commission upon request? What,

[203] *See, e.g.,* 17 CFR 240.17a–1, 240–17a–3, and 17a–4, and 17 CFR 242.301–03.

[204] *Id.*

[205] *See* proposed Rule 818(c).

[206] Nothing in proposed Regulation SBSR would prohibit a SB SEF from serving as the reporting agent on behalf of the counterparty with the obligation to report a trade to the SDR, if the counterparty effected the trade on the SB SEF. *See* Reporting and Dissemination Release, *supra* note 6.

if any, reports or records should the Commission require on a periodic basis? A SB SEF is required to promptly furnish information to the Commission in a manner that is acceptable to the Commission. Are there particular time or format constraints or challenges that the Commission should be aware of with respect to such requests? Would the recordkeeping and reporting requirements be overly burdensome to SB SEFs? If so, why? Or, should the Commission require SB SEFs to provide the Commission direct electronic access to such information and records? Would such direct access be more or less burdensome to SB SEFs than the proposed requirements? If so, what requirements should the Commission consider limiting to reduce the burdens? What would be the basis, if any, to justify reducing the recordkeeping and reporting requirements for SB SEFs that are, as proposed, comparable to requirements for national securities exchanges that also trade SB swaps?

XVI. Core Principle 10—Antitrust Concerns

Section 3D(d)(10) of the Exchange Act (Core Principle 10) [207] provides that, unless necessary or appropriate to achieve the purposes of the Exchange Act, a SB SEF shall not: (1) Adopt any rules or take any actions that result in any unreasonable restraint of trade, or (2) impose any material anticompetitive burden on trading or clearing. The Commission is proposing to implement this Core Principle in proposed Rule 819 by incorporating the statutory language.[208] The Commission requests comment on all aspects of the proposed Rule 819. What do commenters believe would be a "material anticompetitive burden" on trading and clearing? Should the Commission prescribe specific rules or offer guidance to address such situations?

XVII. Core Principle 11—Conflicts of Interest

Section 3D(d)(11) of the Exchange Act (Core Principle 11) requires a SB SEF to establish and enforce rules to minimize conflicts of interest in its decision-making process and establish a process for resolving the conflicts of interest.[209] Pursuant to this directive, the Commission is proposing Rule 820 to mitigate conflicts of interest through governance arrangements applicable to SB SEFs.

The Commission recently proposed new Regulation MC as part of its rulemaking [210] mandated by Section 765 of the Dodd-Frank Act.[211] Section 765 of the Dodd-Frank Act requires the Commission to adopt rules to mitigate specified conflicts of interest relating to SB SEFs, security-based swap clearing agencies, and SBS exchanges.[212] As the Commission explained in the Regulation MC Proposing Release, a conflict of interest could arise when a small number of market participants exercise control or influence over a SB SEF, either through ownership of voting interests or participation in the governance of the SB SEF. When a small group of market participants also dominate much of the trading in SB swaps, control of a SB SEF by these participants raises a heightened concern. Such market participants, through ownership interest in or influence over the governance of a SB SEF, potentially could exercise their influence to limit the number of direct participants in the SB SEF and restrict the scope of SB swaps that are listed for trading on a SB SEF in an effort to limit competition and increase their ability to maintain higher profit margins.[213] The Commission also believes that a SB SEF's ownership and governance structure could create an incentive for behaviors that would promote its owners' commercial interests over its market oversight responsibilities.[214] Each of these potential conflicts of interest could limit the benefits of centralized trading in the SB swap market and potentially undermine the mandatory trading requirement in Section 3C(h) of the Exchange Act, thereby negatively affecting efficiency and competition in the SB swap markets.[215]

Accordingly, the Commission proposed in Regulation MC to, among other things, impose a 20% limit on ownership (based on interests entitled to vote) and voting interest by any direct participants of SB SEFs; require the board of a SB SEF be composed of a majority of independent directors; require a fully independent nominating committee; require a fully independent ROC; and require the SB SEF to inform the Commission when a recommendation of the ROC is not implemented by the board.[216]

As discussed above, in this proposal, the Commission is proposing rules relating to impartial access to SB SEFs and a review process for those SB swaps to be traded on a SB SEF, that are designed to work together with Regulation MC to help mitigate potential conflicts of interest.[217] As described in this section, the Commission also is proposing additional governance rules that are designed to mitigate potential conflicts of interest.[218] The proposed rules in this proposal—regarding both impartial access and governance—seek to address the same conflicts of interest issues as identified in proposed Regulation MC, but using different mechanisms. The Commission will consider both rulemaking proposals as a whole, including how they interact with each other, when considering how best to address these conflicts of interest issues. As requested in detail below, in reviewing the proposed rules, commenters are encouraged to do the same.

The Commission's proposal for SB SEFs is informed by the Commission's experience with national securities exchanges. Historically, national securities exchanges were owned by their members and were structured as

[207] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(10) of the Exchange Act).

[208] As discussed further in Section XVII below, the Commission proposed a number of requirements in Regulation MC designed to mitigate conflicts of interest relating to SB SEFs. The additional rules the Commission is proposing herein are designed to work together with proposed Regulation MC to help mitigate potential conflicts of interest, as identified in the Regulation MC Proposing Release. In addition, as discussed in Section XVII, the Commission is proposing governance rules that also are designed to help mitigate potential conflicts of interest relating to SB SEFs.

The Commission notes that the statutory language of Section 3D(d)(10)(B) of the Exchange Act differs somewhat from the requirements in the Exchange Act relating to national securities exchanges. Section 6(b)(8) of the Exchange Act, 15 U.S.C. 78f(b)(8), requires that the rules of a national securities exchange not impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.

[209] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(11) of the Exchange Act).

[210] *See* Regulation MC Proposing Release, *supra* note 82.

[211] *See* Public Law 111–203, § 765.

[212] *Id.*

[213] *See* Regulation MC Proposing Release, 75 FR at 65890, *supra* note 82.

[214] The Commission notes that an entity that registers as a SB SEF would have oversight responsibility over its market pursuant to the Exchange Act (as amended by the Dodd-Frank Act), and rules adopted thereunder. *See* Public Law 111–203, § 763(c). Similarly, all national securities exchanges, including those that may post or make available for trading SB swaps, have oversight responsibilities over their markets and their members pursuant to the Exchange Act. *See* Section 6 of the Exchange Act, 15 U.S.C. 78(f).

[215] *See* Public Law 111–203, § 763(a). Section 3C(h) of the Exchange Act imposes a mandatory trading requirement, which provides that counterparties shall execute a transaction in a SB swap subject to the clearing requirement of Section 3C(a)(1) on an exchange or a registered SB SEF or a SB SEF that is exempt from registration pursuant to Section 3D(e).

[216] *See* Regulation MC Proposing Release, *supra* note 82.

[217] *See supra* Sections VI and VII.

[218] *See* proposed Rule 820.

not-for-profit or similar organizations.[219] With the advent of shareholder-owned exchanges, the Commission became concerned that the introduction of a class of owner that does not trade on the exchange could exacerbate the possibility that an exchange would put its commercial interests ahead of its responsibilities as a regulator.[220] The Commission also recognizes the potential for any person that directly or indirectly controls an exchange or facility thereof to direct its operation so as to cause the exchange to neglect its regulatory obligations under the Exchange Act or to improperly interfere with or restrict the ability of the Commission to effectively carry out its oversight responsibilities.[221]

The Commission has considered the conflicts between an exchange's regulatory responsibilities and its commercial interests in operating a marketplace for the trading of securities.[222] To address these types of concerns, the Commission has approved proposed procedures, consistent with the requirements of Section 6 of the Exchange Act,[223] for an approach to mitigate conflicts of interest for national securities exchanges through the Commission's review of proposals by exchanges with respect to their ownership [224] and governance structures (generally from member-owned to shareholder-owned organizations) or of applications by entities to register as national securities exchanges.[225] In its review, the Commission has examined the way in which an exchange addresses certain governance principles. Among other things, the Commission looks to assure that an exchange provides fair representation of members in the selection of directors and the administration of its affairs, and provide that one or more directors be representative of issuers and investors and not be associated with a member of the exchange, broker or dealer, consistent with the requirement in Section 6(b)(3) of the Exchange Act.[226]

To complement the governance requirements proposed in Regulation MC, the Commission proposes additional substantive requirements with respect to the governance of SB SEFs that are designed to address the conflict of interest concerns identified above. The Commission proposes that SB SEF participants be provided "fair representation" in the selection of directors of the SB SEF and administration of its affairs. Thus, the proposed rule would require the rules of a SB SEF to assure a fair representation of its participants [227] in the selection of its directors and administration of its affairs, but no less than 20% of the total number of directors of the SB SEF must be selected by the SB SEF's participants.[228] The Commission preliminarily believes that the proposed 20% requirement strikes a proper balance by giving SB SEF participants a practical voice in the governance of the SB SEF and the administration of its affairs, without undermining the overall independence of the Board.[229]

To ensure that SB SEF participants truly have a voice in the selection of directors, the Commission also proposes that SB SEF participants be permitted to participate in the nomination process of such representative directors, with the right to petition for alternative candidates. The proposed rule would require the rules of a SB SEF to establish a fair process for SB SEF participants to nominate an alternative candidate or candidates to the Board by petition and the percentage of SB SEF participants that is necessary to put forth such alternative candidate or candidates.[230] A SB SEF would have some flexibility in implementing a fair process for members to select Board candidates.[231] In adopting such rules, a SB SEF should endeavor to strike an appropriate balance that provides SB SEF participants a practical mechanism to put forth alternative candidates, without jeopardizing the overall integrity of the nominating process. The SB SEF participant candidates, of course, would

[219] A "member" when used with respect to a national securities exchange means (i) any natural person permitted to effect transactions on the floor of the exchange without the services of another person acting as broker, (ii) any registered broker or dealer with which such a natural person is associated, (iii) any registered broker or dealer permitted to designate as a representative such a natural person, and (iv) any other registered broker or dealer which agrees to be regulated by such exchange and with respect to which the exchange undertakes to enforce compliance with the provisions of the Exchange Act, the rules and regulations thereunder, and its own rules. *See* Section 3(a)(3)(A) of the Exchange Act, 15 U.S.C. 78c(a)(3)(A).

[220] *See, e.g.,* Securities Exchange Act Release No. 62158 (May 24, 2010), 75 FR 30082 (May 28, 2010) (order approving the demutalization of CBOE) ("Exchange Act Release No. 62158").

[221] Because ATSs do not have the regulatory obligations that are required of national securities exchanges under the Exchange Act, the Commission has not to date required ATSs to have governance structures that are similar to those of national securities exchanges.

[222] The Commission's recognition of potential conflicts of interest at exchanges and its approach to date in reviewing and approving measures designed to mitigate those conflicts of interest are a useful point of reference as the Commission identifies and develops proposals to mitigate the conflicts of interest potentially faced by SB SEFs as the trading of SB Swaps moves to regulated markets. However, the Commission recognizes that a SB SEF's regulatory obligations are not the same as a national securities exchange's regulatory obligations.

[223] *See* Section 6(b) of the Exchange Act, 15 U.S.C. 78f(b).

[224] The Commission is not proposing rules with respect to ownership and voting limitations for SB SEFs as part of this rulemaking. The Commission has proposed ownership and voting limitations for participants in a SB SEF, as well as for participants in a SBS exchange, as part of Regulation MC. *See* proposed Rule 702 of Regulation MC.

[225] *See, e.g.,* Exchange Act Release No. 62158, *supra* note 220; Securities Exchange Act Release No. 61698 (March 12, 2010), 75 FR 13151 (March 18, 2010) (In the Matter of the Applications of EDGX Exchange, Inc., and EGDA Exchange, Inc. for Registration as National Securities Exchanges; Findings, Opinion, and Order of the Commission) ("Exchange Act Release No. 61698"); Securities Exchange Act Release No. 58375 (August 18, 2008), 73 FR 49498 (August 21, 2008) (In the Matter of the Application of BATS Exchange, Inc. for Registration as a National Securities Exchange; Findings, Opinion, and Order of the Commission) ("Exchange Act Release No. 58375"); and Securities Exchange Act Release No. 53382 (February 27, 2006), 71 FR 11251 (March 6, 2006) (order approving the merger of NYSE and Archipelago and NYSE's demutualization).

[226] 15 U.S.C. 78f(b)(3). Specifically, Section 6(b)(3) of the Exchange Act requires that the rules of an exchange assure a fair representation of its members in the selection of its directors and administration of its affairs, and must provide that one or more directors be representative of issuers and investors and not be associated with a member of the exchange, broker or dealer. 15 U.S.C. 78f(b)(3). Pursuant to Section 6(b)(3), the Commission has approved SRO rules requiring that at least 20% of the directors on the board be selected by exchange members, as well as SRO rules requiring that exchange members be permitted to participate in the nomination process of such representative directors, with the right to petition for alternative candidates. *See, e.g.,* Exchange Act Release No. 58375, 73 FR at 49500, *id* .

[227] *See* proposed Rule 800 (defining the term "participant" as a person that is permitted to directly engage in or effect transactions on the SB SEF).

[228] *See* proposed Rule 820(a). The Commission notes that national securities exchanges have established a 20% member director requirement for their boards of directors. *See, e.g.,* EDGX Exchange, Inc. Amended and Restated Bylaws, Article III, Section 2(a)(iv) and BATS Y-Exchange Amended and Restated by-Laws Article III, Section 2(b)(ii).

The Commission proposes to define the term "Board" as the Board of Directors or Board of Governors of the SB SEF or any equivalent body. *See* proposed Rule 800 under Regulation SB SEF. The proposed definition is substantially identical to that proposed in the Regulation MC Proposing Release with respect to SB SEFs. *See supra* note 82.

[229] Proposed Regulation MC would require that a Board of a SB SEF be composed of a majority of independent directors. *See* proposed Rule 702(c)(1) under proposed Regulation MC and the Regulation MC Proposing Release, *supra* note 82.

[230] *See* proposed Rule 820(c).

[231] The Commission notes that national securities exchanges have implemented the 20% member director requirement by various means. For example, the BATS Y-Exchange, Inc. has a separate member nominating committee that will nominate candidates for each member representative director position on the exchange's board. BATS Global Markets, as the sole shareholder of BATS Y-Exchange, Inc., will elect those candidates nominated by the member nominating committee as member representative directors. *See* BATS Y-Exchange Amended and Restated by-Laws Article III, Section 4.

be required to satisfy all relevant eligibility criteria for directors.

Further, the Commission proposes that SB SEF participant-owners be restricted in their ability to participate in the "fair representation" process. The rules of a SB SEF would therefore require the SB SEF to preclude any SB SEF participant, or any group or class of participants, either alone or together with its related persons, that beneficially owns, directly or indirectly, an interest in the SB SEF from dominating or exercising disproportionate influence in the selection of the fair representation directors if the participant or participants may thereby dominate or exercise disproportionate influence in the selection or appointment of the entire Board.[232] For example, if a group of five participants together owned the SB SEF and, as a result of such ownership, were effectively able to select the directors on the Board of the SB SEF, those owners would be precluded from also being the fair representation directors on the Board. The Commission believes that such a requirement should help mitigate any conflicts of interest that may arise between SB SEF participants who are also owners of the SB SEF. Given the nature of the conflict concerns for the trading of SB swaps and the structure of the SB swaps market—namely, the dominance by a small group of dealers and the concerns with respect to undue influence in the operation of the SB SEF[233]—the Commission believes that it is necessary and appropriate for the Commission to require that a SB SEF take means to prevent a SB SEF participant or group of participants from exerting undue influence in the nomination and selection of the entire Board.

Finally, the Commission proposes that at least one director on the Board of a SB SEF shall be representative of investors who are not SB swap dealers or major SB swap participants and such director must not be a person associated with a SB SEF participant.[234] The Commission believes that requiring representation by investors who are not SB swap dealers or major SB swap participants, or associated with SB SEF participants, would provide an important perspective to the governance and administration of a SB SEF. Investor directors could provide unique and different perspectives from dealers and other participants of the SB SEF, which should enhance the ability of the Board to address issues in an impartial fashion and consequently support the integrity of a SB SEF's governance.

The Commission believes that the proposed governance requirements, described above, are important to help ensure that all SB SEF participants and investors have a voice in the administration and governance of the SB SEF. The proposed requirements should reduce the possibility that a single group of market participants has the ability to unfairly disadvantage other market participants through the SB SEF governance process. Moreover, the proposed requirements for SB SEFs would be consistent with Exchange Act requirements for national securities exchanges.[235] The Commission believes that similar requirements for SB SEFs would help to minimize conflicts of interest in the SB SEF decision-making process.

The Commission requests comments on all aspects of the proposed rules related to governance of the SB SEF. Are there provisions of the proposed rules that are unnecessary or are there other provisions that should be added? If so, why? Are there aspects of the proposed rules that would be difficult for SB SEFs to implement and, if so, why would that be the case?

Should the Commission adopt compositional requirements to provide certain constituencies a guaranteed voice in the selection of the SB SEF's directors and the administration of its affairs, in addition to those proposed? For example, the proposed "fair representation" requirement relates to the fair representation of a SB SEF's participants. Should the requirement instead specifically require fair representation of specific categories of participants, such as SB swap dealers and major SB swap participants? Are there constituencies that commenters believe should be entitled to representation in the election of the Board of a SB SEF that are not addressed in this proposal?

Should the "fair representation" proposal be broadened to include non-participant dealers? Would representation by non-participant dealers be useful to help assure that SB SEFs implement rules and procedures that are designed to provide impartial access? If commenters believe that such representation should be required, should non-participant dealers be provided representation in addition to any required independent directors,[236] or should they be a subset of independent directors?

Are the provisions relating to the "fair representation" requirements appropriate? Should the proposed 20% minimum threshold for "fair representation" be higher or lower? Do commenters agree that it is appropriate for a SB SEF to restrict the ability of a SB SEF participant that is also an owner to dominate or exercise influence in the selection of "fair representation" directors, particularly if the SB SEF would thereby dominate the selection or appointment of the entire Board? If not, why not? If so, why? Is the proposed rule's requirement that the Board include at least one investor representative appropriate? Should SB SEFs be required to have more than one investor representative on its Board? If so, how many, and why?

Should the Commission require a specific percentage of the total number of SB SEF participants to put forth alternative member candidate or candidates by petition that would be required to be set forth in the SB SEF's rules? If so, what percentage would be appropriate? In the SRO Governance Proposing Release, the Commission proposed a threshold of 10% as the percentage of members necessary to put forth an alternative member candidate or candidates for the exchange board of directors.[237] Would a 10% threshold be appropriate for SB SEFs as well? Should investors who are not SB SEF participants be provided with further representation in the governance and administration of a SB SEF beyond representation on the SB SEF Board?[238]

[232] *See* proposed Rule 820(a).

[233] For further discussion of the current structure of the SB swaps market, *see* the Regulation MC Proposing Release, *supra* note 82, at Section III.B.

[234] *See* proposed Rule 820(b). The term "person associated with a participant" is proposed to mean any partner, officer, director, or branch manager of such participant (or any person occupying a similar status or performing similar functions), any person directly or indirectly controlling, controlled by, or under common control with such participant, or any employee of such participant. *See* proposed Rule 800. The proposed definition is substantially identical to the definition of "person associated with a security-based swap execution facility participant" that has been proposed under Regulation MC. *See* proposed Rule 700(t) under Regulation MC and Regulation MC Proposing Release, *supra* note 82.

[235] *See* Section 6(b)(3) of the Exchange Act, 15 U.S.C. 78f(b)(3).

[236] *See* Regulation MC Proposing Release, *supra* note 82.

[237] *See* Securities Exchange Act Release No. 50699 (November 18, 2004), 69 FR 71126 (December 8, 2004) at 71137–71138. *See also, e.g.,* NASDAQ Stock Market LLC, Bylaws, Article II, Section 1(b)(ii) stating that Nasdaq members may submit a petition in support of an alternate candidate (*i.e.,* candidate not selected by the nominating committee) provided that the petition is executed by "10% or more of all Nasdaq Members."

[238] *See* discussion *supra* at Section VIII.B discussing proposed Rule 811(c)(2), which would provide that the SB SEF must establish a swap review committee that would provide for the fair representation of participants of the SB SEF and

Continued

Should the Commission require SB SEFs to have a participation committee that would, for example, determine the standards and requirements for participant eligibility and review denials of participation applications? If so, should there be any requirements as to the composition of such a committee? For example, should any such committee be required to have a majority of independent directors? Would some other percentage of independence be appropriate for a participation committee? Should the Commission require investor representation on a participation committee? If so, should the Commission require a minimum percentage of investor representation and if so what percentage and why?

As noted above, various provisions of proposed Regulation SB SEF, such as the impartial access requirements of proposed Rule 811(b) and the governance requirements of proposed Rule 820 are intended to be complementary measures, along with proposed Regulation MC, designed to mitigate conflicts of interest for SB SEFs. The Commission seeks commenters' views regarding the interaction of proposed Regulation SB SEF with proposed Regulation MC. Taking into account both proposals, commenters should address whether the proposals contained in Regulation SB SEF would appropriately address conflicts of interest concerns or whether they should be revised either as unnecessary or insufficient to address conflicts of interest. Are there any redundancies or gaps for mitigating conflicts of interest that should be addressed?

In reviewing proposed Rule 820 specifically, commenters are asked to consider how this proposed rule would work together with Regulation MC. Are the requirements of proposed Rule 820 and the requirements of Regulation MC mutually supportive? Are any of the requirements of proposed Rule 820 redundant with, or otherwise unnecessary in light of, the proposed requirements of Regulation MC? Are there additional or different measures that the Commission should take to mitigate conflicts of interest? For example, should the Commission require SB SEFs to make publicly available, or available to the Commission but not to the public, Board and committee decisions with respect to the listing of SB swaps? Should the Commission require that the independent directors of the Board conduct and submit to the Commission, or make publicly available, an annual governance self-assessment, which would include ways in which the SB SEF addressed conflicts of interest? If so, are there particular areas that should be the focus of any such annual governance self-assessment? What would be the benefits and drawbacks of any such annual governance self-assessment? Should proposed Form SB SEF require SB SEFs to provide details about the background of each independent director and why it believes that each independent director qualifies as independent? [239]

A number of commenters on Regulation MC raised concerns about the overall approach of, and the proposed requirements in, Regulation MC and expressed a range of views.[240] Several other commenters on Regulation MC, however, generally supported the overall approach to mitigate conflicts of interest and expressed a range of views on the proposed requirements.[241] In particular, the Commission notes that some commenters who have submitted comment letters on proposed Regulation MC raised additional sources of conflicts to consider.[242] These commenters suggested that the Commission should focus on conflicts arising from dealers directing volume to SBS exchanges and SB SEFs, dealer concentration of market activity, and close association of the dealers with decision-making in SBS exchanges and SB SEFs. Namely, the commenters believed that the Commission should address the incentives SB SEFs and SBS exchanges may use to attract business, such as volumetric or profit-based incentives. The commenters argued that if arrangements to attract large liquidity providers' business are overly generous, such arrangements may undermine any improvements made by the proposed voting and ownership limitations and governance requirements in Regulation MC. Do commenters agree with these concerns? If not, why not? If so, do commenters believe that the Commission should take any measures to mitigate these concerns? For example, should the Commission prohibit, or take other measures with respect to, revenue sharing, volume discounts, rebates, and other similar arrangements by a SB SEF to attract order flow? Should SB SEFs be required to file with the Commission any arrangements with participants, potential participants, or other market participants that would promote the sending of order flow to the SB SEF, such as equity incentive plans? Would such requirements help to mitigate conflicts of interest?

XVIII. Core Principle 12—Financial Resources

Section 3D(d)(12)(A) of the Exchange Act (Core Principle 12) requires SB SEFs to have adequate financial, operational, and managerial resources to discharge each responsibility of the SB SEF, as determined by the Commission. In addition, Section 3D(d)(12)(B) of the Exchange Act states that the financial resources of a SB SEF shall be considered to be adequate if the value of the financial resources (i) enables the organization to meet its financial obligations to its members and

other market participants, such that each class of participant and other market participants would be given the right to participate in such committee and no single class of participant or category of market participant would predominate.

[239] *See* Section XXII for a description of proposed Form SB SEF, which would require the disclosure of certain information relating to directors of an SB SEF. Proposed Exhibit C to Form SB SEF would require that an applicant provide a list of the officers and directors of the SB SEF, or persons performing similar functions, who presently hold or have held their offices or positions during the previous year, and a list of all standing committees and their members, indicating the following for each: their name and title; date of commencement and termination of term of office or position; the type of business in which each is primarily engaged (*e.g.,* SB swap dealer, major SB swap participant, inter-dealer broker, end-user *etc.*); and, if such person is a director, whether such director qualifies as an "independent director" pursuant to proposed Rule 800 under Regulation SB SEF and whether such director is a member of any standing committees or committees that have the authority to act on behalf of the Board or the nominating committee.

[240] *See, e.g.,* Letter from Nancy C. Gardner, Executive Vice President & General Counsel, Thomson Reuters Markets, to Elizabeth M. Murphy, Secretary, Commission, dated November 24, 2010, Letter from Lee H. Olesky, Chief Executive Officer, and Douglas L. Friedman, General Counsel, Tradeweb Markets LLC, to David A. Stawick, Secretary, CFTC, dated November 17, 2010, and Letter from Ernest C. Goodrich, Jr., Managing Director, Deutsche Bank AG, and Marcelo Riffaud, Managing Director, Deutsche Bank AG, to Elizabeth M. Murphy, Secretary, Commission, and David A. Stawick, Secretary, CFTC, dated November 8, 2010.

[241] *See, e.g.,* Letter from U.S. Department of Justice, Antitrust Division, In the Matter of: RIN 3235–AK47, File No. S7–27–10, dated December 28, 2010, Letter from Mark Scanlan, Vice President, Agriculture and Rural Policy, Independent Community Bankers of America, to Elizabeth M. Murphy, Secretary, Commission, dated November 26, 2010, and Letter from Laurel Leitner, Senior Analyst, Council of Institutional Investors, to Elizabeth M. Murphy, Secretary, Commission, dated November 19, 2010.

[242] Letter from U.S. Senator Carl Levin, Michigan, to Elizabeth M. Murphy, Secretary, Commission, dated December 20, 2010; Letter from Dennis M. Kelleher, President & CEO, and Wallace C. Turbeville, Derivatives Specialist, Better Markets, Inc. to Elizabeth M. Murphy, Secretary, Commission, dated November 26, 2010; Letter from U.S. Senator Sherrod Brown, Ohio, to Elizabeth M. Murphy, Secretary, Commission, and David A. Stawick, Secretary, CFTC, dated November 17, 2010; Letter from U.S. Senator Tom Harkin, Iowa, to Elizabeth M. Murphy, Secretary, Commission, and David A. Stawick, Secretary, CFTC, dated November 17, 2010; and Letter from Americans for Financial Reform, to Elizabeth M. Murphy, Secretary, Commission, dated November 16, 2010.

participants notwithstanding a default by the member or participant creating the largest financial exposure for that organization in extreme but plausible market conditions; and (ii) exceeds the total amount that would enable the SB SEF to cover the operating costs of the SB SEF for a one year period, as calculated on a rolling basis. The Commission believes that the financial strength of a SB SEF is vital to ensure that a SB SEF can discharge its regulatory responsibilities in accordance with the Exchange Act. Strong, viable SB SEFs will be a key to market continuity and efficiency. Therefore, the Commission believes that it is important to install safeguards to ensure that a SB SEF's resources are adequate.

The Commission proposes to implement in proposed Rule 821 the requirements of Section 3D(d)(12) of the Exchange Act. Specifically, proposed Rule 821(a) would require every SB SEF to have adequate financial, operational, and managerial resources to discharge each responsibility of the SB SEF, as determined by the Commission. Proposed Rule 821(b) would state in part that the financial resources of a SB SEF shall be considered to be adequate if the value of the financial resources enables the SB SEF to meet its financial obligations to participants notwithstanding a default by the participant creating the largest financial exposure for the SB SEF in extreme but plausible market conditions. This requirement would help ensure that the financial failure of one participant would not be able to destroy the financial viability of the entire SB SEF. Proposed Rule 821(b) would require that in making this calculation (which is required by Section 3D(d)(12)(B) of the Exchange Act), a SB SEF shall use reasonable estimates and assumptions and not overestimate resources or underestimate expenses, liabilities, and financial exposure. This requirement should provide guidance to SB SEFs on the estimates they should use to comply with the requirements of Core Principle 12.

Proposed Rule 821(b) also would state in part that the financial resources of a SB SEF shall be considered to be adequate if the value of the financial resources exceeds the total amount that would enable the SB SEF to cover its operating costs for a one year period, as calculated on a rolling basis. This test would help to ensure that a SB SEF is in a sufficiently strong financial position to sustain operations through unpredictable business cycles. As with the first requirement, in making this calculation (which is required by Section 3D(d)(12)(B) of the Exchange Act), a SB SEF must use reasonable assumptions and estimates and not overestimate resources or underestimate expenses, liabilities, and financial exposure. Each of these requirements would be an ongoing requirement and a SB SEF must always be in compliance.[243] The Commission seeks comments in general regarding all aspects of these financial requirements.

XIX. Core Principle 13—Systems Safeguards

Section 3D(d)(13)(A) of the Exchange Act (Core Principle 13) requires that a SB SEF shall establish and maintain a program of risk analysis and oversight to identify and minimize sources of operations risk, through the development of appropriate controls and procedures, and automated systems, that: (1) Are reliable and secure and (2) have adequate scalable capacity. Additionally, Section 3D(d)(13)(B) of this Core Principle requires that a SB SEF establish and maintain emergency procedures, backup facilities, and a plan for disaster recovery that allow for: (1) Timely recovery and resumption of operations and (2) the fulfillment of the responsibilities and obligations of the SB SEF. Further, Section 3D(d)(13)(C) of this Core Principle requires that a SB SEF shall periodically conduct tests to verify that the backup resources of the SB SEF are sufficient to ensure continued: (1) Order processing and trade matching, (2) price reporting, (3) market surveillance, and (4) maintenance of a comprehensive and accurate audit trail. The Commission is proposing Rule 822 to implement this Core Principle.

The Commission is proposing Rule 822 to provide standards for SB SEFs with regard to their automated systems' capacity, resiliency, and security.[244] These standards are comparable to the standards applicable to SROs, including national securities exchanges and clearing agencies, pursuant to the Commission's Automation Review Policy ("ARP") standards.[245] Systems failures can limit access to quotes or other trading interest, call into question the integrity of quotes or other trading interest, and prevent market participants from being able to post quotes or other trading interest, and thereby have a large impact on market confidence, risk exposure, and market efficiency. To promote the maintenance of stable and orderly SB swap markets, the Commission believes that SB SEFs should be required to meet the ARP capacity, resiliency and security standards.[246]

Proposed Rule 822 would require a SB SEF to establish, maintain, and enforce written policies and procedures designed to ensure that its systems provide adequate levels of capacity, resiliency, and security; and submit to the Commission annual reviews of its automated systems, systems outage notices, and prior notices of planned system changes. These proposed requirements essentially codify and parallel the ARP requirements that have been in place for almost twenty years. Commission staff has found these standards to be effective in overseeing the capacity, resiliency, and security of major automated systems in use in the securities markets. These proposed requirements, as applied to the market for SB swaps, are designed to prevent and minimize the impact of systems failures that might negatively impact the stability of this market.

A. Requirements for SB SEFs' Automated Systems

1. Policies and Procedures

Proposed Rule 822(a)(1) would require a SB SEF to establish, maintain, and enforce written policies and procedures reasonably designed to ensure that its systems provide adequate levels of capacity, resiliency, and security. Such policies and procedures would require a SB SEF to, at a minimum: (1) Establish reasonable current and future capacity estimates; (2) conduct periodic capacity stress tests of critical systems to determine such systems' ability to process transactions in an accurate, timely, and efficient manner; (3) develop and implement reasonable procedures to review and keep current its system development and testing methodology; (4) review the

[243] In addition to the requirements of proposed Rule 821, a SB SEF would be required to submit annual financial reports in accordance with the requirements discussed in Section XXII of this release.

[244] Proposed Rule 822 is being promulgated under Section 3D(d)(13) of the Exchange Act.

[245] *See* Securities Exchange Act Release Nos. 27445 (Nov. 16, 1989), 54 FR 48703, 48706–48707 (November 24, 1989) ("ARP I Release") and 29185 (May 9, 1991), 56 FR 22490 (May 15, 1991) ("ARP II Release"). *See also* Rule 301(b)(6) of Regulation ATS, 17 CFR 242.301(b)(6) and Securities Exchange Act Release No. 40760 (Dec. 8, 1998), 63 FR 70844 (December 22, 1998).

[246] Because SB SEFs would be an integral part of the market for SB swaps, and therefore an integral part of the national market system, the Commission believes that it is appropriate to model a SB SEF's rules on system safeguards on ARP. Proposed Rule 822 will impose data maintenance standards on SB SEFs that are comparable to those imposed by the Commission on national securities exchanges by applying the ARP standards to them. In addition, nearly identical rules have been proposed by the Commission for SDRs, also applying the ARP standards to those entities. *See* SDR Release, *supra* note 6.

vulnerability of its systems and data center computer operations to internal and external threats, physical hazards, and natural disasters; and (5) establish adequate contingency and disaster recovery plans which shall include plans to resume trading of SB swaps by the SB SEF no later than the next business day following a wide-scale disruption. In developing such contingency and disaster recovery plans, the SB SEF would be required to take into account: (1) The extent of alternative trading venues for the SB swaps traded by the SB SEF, including the number of SB swaps traded on the SB SEF, the market share of the SB SEF, and the number of participants in its SB SEF; and (2) the necessity of geographic diversity and diversity of infrastructure between the SB SEF's primary site and any back-up sites.

This list of proposed requirements is based on existing ARP requirements applied to significant-volume ATSs under Rule 301(b)(6) of Regulation ATS.[247] In addition, Commission staff has applied these requirements to SROs and other entities in the securities markets for a number of years in the context of its ARP inspection program.

As a general matter, the Commission preliminarily believes that, if a SB SEF's policies and procedures satisfy industry best practices standards, then these policies and procedures would be adequate for purposes of proposed Rule 822(a)(1).[248] However, in the event that industry best practices standards of widely recognized professional organizations are not consistent with the public interest, protection of investors, or the maintenance of fair and orderly markets, the Commission would have flexibility to establish such standards that a SB SEF would be required to meet to comply with proposed Rule 822(a)(1).[249]

The proposed rule would require a SB SEF to quantify, in appropriate units of measure, the limits of the SB SEF's capacity to receive (or collect), process, store, or display the data elements included within each function, and identify the factors (mechanical, electronic, or other) that account for the current limitations.[250] This would make it easier for the Commission to detect any potential capacity constraints of a SB SEF, which, if left unaddressed, could compromise the ability of a SB SEF to collect and maintain SB swap data. A SB SEF's failure to clearly understand and have procedures to address its capacity limits would increase the likelihood that it would experience a loss or disruption of system operations.

2. Objective Review

Proposed Rule 822(a)(2) would require a SB SEF to submit an objective review of its systems that support or are integrally related to the performance of its activities to the Commission, on an annual basis, within thirty calendar days of completion. This proposed requirement is critical to help ensure that SB SEFs have adequate capacity, resiliency, and security and that their automated systems are not subject to critical vulnerabilities. Proposed Rule 800 would define "objective review" as "an internal or external review, performed by competent, objective personnel following established procedures and standards, and containing a risk assessment conducted pursuant to a review schedule."[251] The proposed definition of "objective review" is based on the standard for the review of automated systems set forth in the ARP II Release.[252]

As in the current ARP program, the Commission preliminarily believes that a reasonable basis for determining that a review is objective for purposes of proposed Rule 822(a)(2) is if the level of objectivity of a SB SEF's reviewers complied with standards set by widely recognized professional organizations.[253] However, in the event that industry best practices standards of widely recognized professional organizations are not consistent with the public interest, protection of investors, or the maintenance of fair and orderly markets, the Commission would have flexibility to establish standards that a SB SEF would be required to meet to comply with proposed Rule 822(a)(2).

The decision on which type of reviewer, an internal department or an external firm, should perform the review is a decision for each SB SEF to make. The Commission preliminarily believes that, as long as the reviewer has the competence, knowledge, consistency, and objectivity sufficient to perform the role, the review can be performed by either recognized information technology firms or by a qualified internal department knowledgeable of information technology systems.

Proposed Rule 822(a)(2) would further require that, where the objective review is performed by an internal department, an objective, external firm must assess the internal department's objectivity, competency, and work performance with respect to the review performed by the internal department. Proposed Rule 822(a)(2) would require that the external firm issue a report of that review, which the SB SEF must submit to the Commission on an annual basis, within thirty calendar days of completion of the review.

The proposed requirement in proposed Rule 822(a)(2) that a SB SEF submit an annual objective review to the Commission is drawn from the ARP II Release.[254] In addition, the proposed requirement in proposed Rule 822(a)(2) that, where the objective review is performed by an internal department, an objective, external firm must assess the internal department's objectivity, competency, and work performance, is similarly drawn from the ARP II Release.[255]

The proposed annual review would not be required to address each element contained in proposed paragraphs (i) through (v) of Rule 822(a)(1) every year.

[247] *See* 17 CFR 242.301(b)(6)(D)(ii).

[248] Proposed Rule 822(a)(1) would require a SB SEF to establish, maintain, and enforce written policies and procedures reasonably designed to ensure that its systems provide adequate levels of capacity, resiliency, and security. A SB SEF's policies and procedures may still meet the requirement to be reasonably designed to ensure that its systems provide adequate levels of capacity, resiliency, and security without necessarily being identical to industry best practices standards. However, generally speaking, industry best practices standards would provide an objective, easily identifiable standard.

[249] Industry best practices standards currently are established by organizations such as: the Information Systems Audit and Control Foundation ("ISACF"); the Federal Financial Institutions Examination Council's ("FFIEC"); the Institute of Internal Auditors ("IIA"); and the SANS Institute.

[250] *See* proposed Rule 822(a)(1)(i).

[251] Proposed Rule 800 would define "competent, objective personnel" as "a recognized information technology firm or a qualified internal department knowledgeable of information technology systems." This proposed definition is based on the standard for reviewers of automated systems set forth in the ARP II Release. *See* ARP II Release, 56 FR 22490, *supra* note 245. Proposed Rule 800 would define "review schedule" as "a schedule in which each element contained in paragraph (a)(1) of Rule 822 would be assessed at specific, regular intervals." This proposed definition codifies the Commission's policy set forth in the ARP II Release. *See* ARP II Release, 56 FR 22490, *supra* note 245.

[252] *See* ARP II Release, 56 FR 22490, *supra* note 245.

[253] Such standards are currently established by organizations such as the IIA, the Information Systems Audit and Control Association ("ISACA") (formerly the Electronic Data Processing Auditors Association ("EDPAA")), and the American Institute of Certified Public Accountants ("AICPA").

Proposed Rule 822(a)(2) would require a SB SEF to submit an objective review of its systems that support or are integrally related to the performance of its activities to the Commission, on an annual basis, within thirty calendar days of completion. A SB SEF's policies and procedures may still meet this requirement without necessarily being identical to industry best practices standards. However, generally speaking, industry best practices standards would provide an objective, easily identifiable standard.

[254] *See* ARP II Release, 56 FR 22490, *supra* note 245.

[255] *See id.*

Rather, using its own risk assessment, a SB SEF's reviewer would review each element on a "review schedule," as defined in proposed Rule 800, in which each element would be assessed at specific, regular intervals, thus facilitating systematic and timely review of each element. This should provide a reasonable and cost-effective level of assurance that automated systems of SB SEFs are being adequately developed and managed with respect to capacity, security, development, and contingency planning concerns.

The proposed requirement to submit an objective review within thirty days of completion assures the Commission will have timely notice of the information required. The Commission has found through its experience with the current ARP program for SROs and other entities in the securities market that an entity generally requires approximately thirty calendar days after completion of the review to complete the internal review process necessary to submit an annual review to the Commission. A shorter timeframe might not provide a SB SEF with sufficient time to complete its internal review of the document; a longer timeframe might serve to encourage unnecessary delays.

3. Material Systems Outages

Under proposed paragraph (3) of Rule 822(a), a SB SEF would be required to promptly notify the Commission in writing of material system outages and any remedial measures that have been implemented or are contemplated, including: (1) Immediately notifying the Commission when a material systems outage is detected; (2) immediately notifying the Commission when remedial measures are selected to address the material systems outage; (3) immediately notifying the Commission when the material systems outage is addressed; and (4) submitting to the Commission within five business days of when the material systems outage occurred a detailed written description and analysis of the outage and any remedial measures that have been implemented or are contemplated.

This paragraph would codify the procedures followed by SROs and certain other entities under the Commission's current ARP program with respect to providing the staff with notification of material system outages. In particular, proposed paragraph (3) would clarify that the Commission expects to receive immediate notification that an outage has been detected, that remedial measures have been selected to address the outage, and that the outage has been addressed. Proposed paragraph (3) also would clarify that a SB SEF should submit a detailed written description and analysis of the outage within five business days of the occurrence of the outage.

The Commission preliminarily believes that the proposed rule would assist the Commission in assuring that a SB SEF has diagnosed and is taking steps to correct system disruptions, so that systems of the SB SEF are reasonably equipped to accept and securely maintain transaction data. The Commission preliminarily believes that requiring a SB SEF to submit notifications of material system outages to the Commission is essential to help ensure that the Commission can continue to effectively oversee the SB SEF.

Proposed Rule 800 would define "material systems outage" as an unauthorized intrusion into any system, or an event at a SB SEF involving systems or procedures that results in: (1) A failure to maintain accurate, time-sequenced records of all orders, quotations, and transactions that are received by, or originated on, the SB SEF; (2) a disruption of normal operations, including switchover to back-up equipment with no possibility of near-term recovery of primary hardware; (3) a loss of use of any system; (4) a loss of transactions; (5) excessive back-ups or delays in processing; (6) a loss of ability to disseminate vital information; (7) a communication of an outage situation to other external entities; (8) a report or referral of an event to the SB SEF's Board or senior management; (9) a serious threat to systems operations even though systems operations were not disrupted; (10) a queuing of data between system components or queuing of messages to or from participants of such duration that a participant's normal service delivery is affected; or (11) a failure to maintain the integrity of systems that results in the entry of erroneous or inaccurate inquiries, responses, orders, quotations, other trading interest, transactions, or other information in the SB SEF or the securities markets.

Based on its experience in requiring SROs and other entities to report material systems outages in the context of the current ARP program, the Commission preliminarily believes that this proposed definition is appropriate for SB SEFs. The Commission preliminarily believes that each of the events listed in paragraphs (1) through (11) of proposed Rule 800 are significant events that warrant reporting to the Commission because such material systems outages could negatively impact the stability of the SB swap market. The application of the proposed definition is relatively straightforward, and it focuses on the types of events that the Commission preliminarily believes should require notification to the Commission under proposed Rule 822(a)(3), so that the Commission can respond appropriately to the event that caused the loss or disruption.

Specifically, the Commission preliminarily believes that proposed paragraphs (1), (2), (3), (4), and (5) of proposed Rule 800 address events that cause a significant loss or disruption of normal system operations sufficient to warrant notification to the Commission. In addition, the Commission preliminarily believes that proposed paragraph (6) of proposed Rule 800 addresses a type of event that impairs transparency or accurate and timely regulatory reporting.

The Commission also preliminarily believes that proposed paragraphs (7) and (8) of proposed Rule 800 are appropriate because communications of an outage to entities outside of the SB SEF or to the SB SEF's Board or senior management are indicia of a significant system outage sufficient to warrant notification to the Commission. Specifically, proposed paragraph (8)'s reference to "a report or referral of an event * * *" seeks to address situations in which a SB SEF might seek to apply an overly narrow definition of an "outage situation" in proposed paragraph (7), in order to avoid reporting a problem that nevertheless has a significant impact on the performance of the SB SEF's systems and therefore warrants reporting to the Commission. For example, where a SB SEF experiences a slowing, but not a stoppage, of its ability to accept orders or quotes, and that slowing is sufficiently significant to have been reported or referred to the SB SEF's Board or senior management, the Commission preliminarily believes that this situation would constitute a material system outage under proposed paragraph (8) that must be reported to the Commission. By including proposed paragraph (8) in the definition of "material systems outage," the Commission seeks to ensure that it is informed of events that most entities subject to current ARP standards would already understand should be covered under the current program. This should permit the Commission to effectively monitor the operation of SB SEF's automated systems. The Commission preliminarily believes that proposed paragraphs (9) and (10) are appropriate because threats to system operations and queuing of data are events that may

result in a significant disruption of normal system operations warranting notification to the Commission.

Proposed paragraph (11) of proposed Rule 800 covers a failure to maintain the integrity of systems that results in the entry of erroneous or inaccurate inquiries, responses, orders, quotations, other trading interests, transactions, or other information in a SB SEF or to market participants. This paragraph is designed to address the unique role of SB SEFs in the SB swaps market. In particular, it is intended to cover such events as breakdowns in a SB SEF's internal controls that result in the entry of erroneous orders into the market. For example, it is possible that a SB SEF could, while in the process of testing its systems, inadvertently retain "test" data in its database. This, in turn, could result in erroneous reporting of SB swaps to the SB SEF's participants, registered SDRs, the Commission, other regulators, and counterparties. Counterparties may become uncertain of their positions, leading to market disruptions. This, in turn, could erode investor confidence in the integrity of the SB swaps market, damaging liquidity and impeding the capital formation process. Accordingly, the Commission preliminarily believes that this type of breakdown in a SB SEF's systems controls should be reported to the Commission.

By including proposed paragraph (11) of proposed Rule 800 in the definition of "material systems outage," the Commission is seeking to ensure that it is informed of events that could negatively impact the integrity of systems that result in the entry of erroneous or inaccurate transaction data or other information in a SB SEF or the securities markets. This should permit the Commission to monitor effectively the operation of each SB SEF's automated systems.

The definition of material systems outage also includes an unauthorized intrusion into any system. This includes unauthorized intrusions by outside parties, insiders, or parties unknown. The Commission preliminarily believes that including this in the definition would assist the Commission's review by requiring SB SEFs to notify the Commission of unauthorized intrusions into systems or networks, and should permit the Commission to continue to effectively monitor the operation of SB SEF's automated systems. SB SEFs would need to immediately report unauthorized intrusions regardless of whether the intrusions were part of a cyber attack, potential criminal activity, other unauthorized attempts to retrieve, manipulate or destroy data or to disrupt or destroy systems or networks, or any other malicious activity affecting data, systems, or networks. If unauthorized intrusions were successful in breaching systems or networks, SB SEFs would need to report these intrusions even if the parties conducting the unauthorized intrusion were unsuccessful in achieving their apparent goals (such as the introduction of malware or other means of disrupting or manipulating data, systems, or networks). SB SEFs would need to follow up on their initial reports by sending the Commission updates on any harm to data, systems, or networks as well as any remedial measures that the SB SEFs are contemplating or undertaking to address the unauthorized intrusions. SB SEFs, however, would not need to report unsuccessful attempts at unauthorized intrusions that did not breach systems or networks.

The Commission preliminarily believes that the proposed five business day requirement regarding submission of a written description of material systems outages is an appropriate time period. In the Commission's experience with the current ARP program for SROs and other entities in the securities market, an entity generally requires approximately five business days after the occurrence of a material systems outage to gather all the relevant details regarding the scope and cause of the outage. A shorter timeframe might not provide sufficient time for the SB SEF to gather all relevant details surrounding the outage and describe them in a written submission; a longer timeframe might encourage unnecessary delays.

4. Material Systems Changes

Under proposed paragraph (4) of Rule 822(a), a SB SEF would be required to notify the Commission in writing at least thirty calendar days before implementation of any planned material systems changes. Proposed Rule 800 would define "material systems change" as "a change to automated systems that: (1) Significantly affects existing capacity or security; (2) in itself, raises significant capacity or security issues, even if it does not affect other existing systems; (3) relies upon substantially new or different technology; (4) is designed to provide a new service or function; or (5) otherwise significantly affects the operations of the security-based swap execution facility."

Based on its experience in requiring SROs and other entities to report material systems changes in the context of the current ARP program, the Commission preliminarily believes that this proposed definition is appropriate for SB SEFs. Each of the events listed in paragraphs (1) through (5) are significant events that warrant reporting to the Commission because any of those events can lead to a material systems outage that could negatively affect the stability of the SB swap market. The application of the proposed definition is relatively straightforward, and it focuses on the types of events that should require notification to the Commission under proposed Rule 822(a)(4). Specifically, the proposed paragraphs (1) through (4) are events that concern the adequacy of capacity estimates, testing, and security measures taken by a SB SEF, and thus are sufficiently significant to warrant notification to the Commission. Proposed paragraph (5) covering a change that "otherwise significantly affects the operations of the security-based swap execution facility" is more open-ended in order to require notification of other major systems changes. Examples of changes that fall within proposed paragraph (5) include, but are not limited to: Major systems architectural changes; reconfigurations of systems that cause a variance greater than five percent in throughput or storage;[256] introduction of new business functions or services; material changes in systems; changes to external interfaces; changes that could increase susceptibility to major outages; changes that could increase risks to data security; changes that were, or will be, reported to or referred to a SB SEF's Board or senior management; and changes that may require allocation or use of significant resources.

The Commission preliminarily believes that the proposed thirty calendar day requirement regarding pre-implementation written notification to the Commission of planned material systems changes is an appropriate time period. The Commission has found through its experience with the current ARP program that this amount of time is necessary for the Commission staff to evaluate the issues raised by a planned material systems change. A shorter timeframe might not provide sufficient time for the Commission staff to analyze the issues raised by the systems change; a longer timeframe might unnecessarily delay the covered entity in implementing the change.

[256] The Commission has identified the five percent threshold as triggering the definition of "material systems change" in proposed Rule 800 because, based on experience in administrating the ARP program in the equities markets for almost twenty years, it believes that reconfigurations that exceed five percent in throughput or storage typically have the greatest potential to cause significant disruptions to automated systems.

The Commission requests comment on all aspects of proposed Rule 822(a). Should the Commission consider imposing other requirements or standards? Should any of the proposed requirements be eliminated or refined? If so, please explain your reasoning. Would it be appropriate to impose the proposed systems safeguards requirements on SB SEFs only after they account for a certain percentage of the total volume of transactions, as measured by the aggregate total volume received by all SB SEFs? If so, what is the appropriate volume level? Five percent? Ten percent? Please be specific. In addition, the Commission is mindful of the potential costs of a SB SEF's compliance with the proposed systems safeguards and seeks commenters' views on whether there are ways to minimize those costs while assuring adequate systems safeguards.

Would it be appropriate to delay implementing the proposed systems safeguards requirements on SB SEFs until after a specified period of time, such as one year after Commission approval of the SB SEF's registration? If so, is one year an appropriate time period? If not, what would be an appropriate time period for any delay and why? Would it be appropriate to delay implementation of systems safeguard requirements until either a specified time period after the Commission's approval of the SB SEF's registration and/or a particular volume threshold such as those discussed above is reached? If so, why? If not, why not? Are there other circumstances in which a SB SEF should be excepted from systems safeguards requirements? If so, commenters should provide a rationale.

Are there factors specific to SB swap transactions that would make applying a system that is traditionally used in the equity markets inappropriate? What is the likely impact of these requirements on the SB swaps market, including the impact on the incentives and behaviors of SB SEFs, the willingness of persons to register as SB SEFs, and the technologies used for maintaining SB swap data at the SB SEF?

Should the Commission require a SB SEF's contingency and disaster recovery plans (required in proposed paragraph (a)(1)(v) of proposed Rule 822) to be tested periodically to assure their effectiveness and adequacy? [257] Should the Commission require such contingency and disaster recovery plans to cover at a minimum: Preparation for contingencies through such devices as appropriate remote and on-site hardware back-up and periodic duplication and off-site storage of data files? Off-site storage of up-to-date, duplicative software, files and critical forms and supplies needed for processing operations, including a geographically diverse back-up site that does not rely on same infrastructure components (*e.g.,* transportation, telecommunications, water supply, and electric power) as the SB SEF primary operations center? Immediate availability of software modifications, detailed procedures, organizational charts, job descriptions, and personnel for the conduct of operations under a variety of possible contingencies? Emergency mechanisms for establishing and maintaining communications with participants, regulators and other entities involved? [258]

Should the Commission require a SB SEF's contingency and disaster recovery plans (required in proposed paragraph (a)(1)(v) of proposed Rule 822) to include resources, emergency procedures, and backup facilities sufficient to enable timely recovery and resumption of its operations following any disruption of its operations? If so, what should the recovery time objective be? Should the SB SEF's contingency and disaster plans and resources generally enable resumption of the SB SEF's operations during the next business day following the disruption?

Should the Commission require a SB SEF, to the extent practicable, coordinate its contingency and disaster recovery plans (required in proposed paragraph (a)(1)(v) of proposed Rule 822) with those of the SDRs, clearing agencies, SB swap dealers, and major SB swap participants, and with those of regulators in a manner adequate to enable effective resumption of the SB SEF's operations following a disruption causing activation of the SB SEF's contingency and disaster recovery plans, including participating in periodic, synchronized testing of its contingency and disaster recovery plans?

Should the Commission require a SB SEF ensure that its contingency and disaster recovery plans (required in proposed paragraph (a)(1)(v) of proposed Rule 822) take into account the business continuity-disaster recovery plans of its telecommunications, power, water, and other essential service providers?

Should the Commission require a SB SEF to identify the potential risks that can arise as a result of interoperability and/or interconnectivity with other market infrastructures and venues from which data can be submitted to the SB SEF (such as exchanges, SDRs, clearing agencies, SB swap dealers, and major SB swap participants) and service providers and how the SB SEF mitigates such risks?

Should the Commission require a SB SEF to abide by substantive requirements (in addition to, or in place of, the policies and procedures approach of proposed Rule 822(a)(1)), such as (i) having robust system controls and safeguards to protect the data from loss and information leakage, (ii) having high-quality safeguards and controls regarding the transmission, handling, and protection of data to ensure the accuracy, integrity, and confidentiality of the trade information recorded in the SB SEF, or (iii) having reliable and secure systems and having adequate, scalable capacity?

Should the Commission require a SB SEF to establish, maintain, and enforce written policies and procedures reasonably designed to ensure that the transaction data that it accepts is from the entity it purports to be from, such as requiring robust passwords?

Are the time periods specified in proposed Rule 822(a)(2) through (4) with respect to submission of annual reviews and written notices of material system outages and material systems changes the correct time periods to use? Should any of the proposed time periods be shortened or lengthened? Should the time periods be replaced with less specific requirements, such as "promptly" or "timely"? If so, please explain your reasoning.

Should the Commission require the notification required by proposed Rule 822(a)(4) to be sufficiently detailed to explain the new system development process, the new configuration of the system, its relationship to other systems, the timeframes or schedule for installation, any testing performed or planned, and an explanation on the impact of the change on the SB SEF's capacity estimates, contingency protocols and vulnerability estimates? [259]

Are there specific provisions in the proposed definitions that should be eliminated or refined? Are there some events which should be included in the

[257] This requirement would be similar to what is required of clearing agencies and proposed to be required of SDRs. *See* Exchange Act Release No. 16900 (June 17, 1980), 45 FR 41920 (June 20, 1980) and SDR Release, *supra* note 6.

[258] These requirements are similar to requirements related to disaster recovery plans of clearing agencies and proposed to be required of SDRs. *See id.* and SDR release, *supra* note 6. The requirement for geographical diversity is currently applicable to securities firms. *See* Exchange Act Release No. 47638 (April 7, 2003), 68 FR 17809 (April 11, 2003) (the "BCP Whitepaper").

[259] *See* ARP II Release, 56 FR 22490, *supra* note 245.

definitions of "material systems outage" and "material systems change" that are not, or events that should not be included in these definitions but are? If so, please explain your reasoning.

Are the definitions "objective review" and "competent, objective personnel" parallel to the requirements for SROs and other entities in the securities markets in the context of the current ARP program? Should the objective review required in proposed Rule 822(a)(2) be done on a regular, periodic basis, rather than on an annual basis?

The proposed requirement for an objective review focuses on a review of the SB SEF's automated systems that support or are integrally related to the performance of its activities. Is this an appropriate scope, or should other aspects of the SB SEF's operations be included? If so, which? In addition is this scope sufficiently understandable or should it be further defined?

Is the requirement in proposed Rule 822(a)(2) for an objective, external firm to assess the objectivity, competency, and work performance of an internal department that performed an objective review necessary or appropriate? If the objective review is done by an internal department, should the Commission require that the objective review be done by a department or persons other than those responsible for the development or operation of the systems being tested?

Do the proposed requirements for SB SEFs establish sufficient criteria against which an evaluation can be performed by a third party? If not, should the Commission impose a specific framework for the SB SEFs to use in establishing automated systems and related controls? If so, what would the critical components of the framework include? Are existing frameworks available that are suitable for this purpose and, if so, which ones would be considered appropriate?

Should the Commission require the use of a specific framework by outside or inside parties for evaluating whether SB SEFs have adequate capacity, resiliency, and security and that their automated systems are not subject to critical vulnerabilities? If so, what would the critical components of the framework include? Are existing frameworks available that are suitable for this purpose and, if so, which ones would be considered appropriate?

For reviews performed by internal audit departments, are the requirements for an external firm involvement appropriate? If not, what improvements could be made to promote appropriate reviews by external firms in these circumstances?

B. Electronic Filing

Proposed Rule 822(b) would require that every notification, review, or description and analysis required to be submitted to the Commission under proposed Rule 822 be submitted in an appropriate electronic format to the Office of Market Operations at the Division of Trading and Markets at the Commission's principal office in Washington, DC. This proposed requirement is intended to make proposed Rule 822 consistent with electronic-reporting standards set forth in other Commission rules under the Exchange Act, such as Rule 17a—-25 (Electronic Submission of Securities Transaction Information by Exchange Members, Brokers, and Dealers) [260] and Rule 19b–4 (Filings with respect to Proposed Rule Changes by Self-regulatory Organizations).[261]

The Commission preliminarily believes that the proposed provision would benefit SB SEFs by automating the process by which they submit notifications, reviews, and descriptions and analyses under proposed Rule 822 to the Commission. The Commission currently receives this type of information from SROs and other entities in the securities market in electronic format. Moreover, as noted above, this provision is intended to be consistent with other Commission rules.

Proposed Rule 822(b) would require submission of notifications, reviews, and descriptions and analyses in an "appropriate electronic format." The Commission anticipates that, if the provision is adopted, the staff would work with SB SEFs to determine appropriate electronic formats that could be used.

The Commission requests comment on all aspects of proposed Rule 822(b) as well as on the following specific issues. Are there specific provisions in proposed Rule 822(b) that should be eliminated or refined? If so, please explain your reasoning.

What is the likely impact of this requirement on the SB swap market, including the impact on the incentives and behaviors of SB SEFs, the willingness of persons to register as SB SEFs, and the technologies used for reporting information to the Commission?

C. Confidential Treatment

Proposed Rule 822(c) would provide that a person who submits a notification, review, or description and analysis pursuant to this Rule for which he or she seeks confidential treatment should clearly mark each page or segregable portion of each page with the words "Confidential Treatment Requested." Proposed Rule 822(c) would state that "[a] notification, review, or description and analysis submitted pursuant to this [Rule] will be accorded confidential treatment to the extent permitted by law."

The Commission would use the information collected under proposed Rule 822 to evaluate whether SB SEFs are reasonably equipped to handle market demand. For this reason, requiring SB SEFs to submit this information would be critical to the Commission's ability to effectively oversee SB SEFs.

Much of the information that the Commission expects to receive from SB SEFs under proposed Rule 822 is, by its nature, competitively sensitive. If the Commission were unable to afford confidential protection to the information that it expects to receive, then the SB SEFs may hesitate to submit the required information to the Commission. This result could potentially undermine the Commission's ability effectively to oversee SB SEFs, which, in turn, could undermine investor confidence in the SB swap market.

The Freedom of Information Act ("FOIA") provides at least two exemptions under which the Commission has authority to grant confidential treatment for the information submitted under proposed Rule 822. First, FOIA Exemption 4 provides an exemption for "trade secrets and commercial or financial information obtained from a person and privileged or confidential." [262] As specified in proposed Rule 822(c), "a notification, review, or description and analysis submitted pursuant to this [Rule] will be accorded confidential treatment to the extent permitted by law." The information required to be submitted to the Commission under proposed Rule 822 may contain proprietary information regarding automated systems that is privileged or confidential and thus subject to protection from disclosure under Exemption 4 of the FOIA.

Second, FOIA Exemption 8 provides an exemption for matters that are "contained in or related to examination, operating, or condition reports prepared by, on behalf of, or for the use of an agency responsible for the regulation or supervision of financial institutions." [263] Similarly, Commission Rule 80(b)(8), Commission Records and Information,

[260] 17 CFR 240.17a–25.

[261] 17 CFR 240.19b–4.

[262] 5 U.S.C. 552(b)(4).

[263] 5 U.S.C. 552(b)(8).

implementing Exemption 8, states that the Commission generally will not publish or make available to any person matters that are "[c]ontained in, or related to, any examination, operating, or condition report prepared by, on behalf of, or for the use of, the Commission, any other Federal, State, local, or foreign governmental authority or foreign securities authority, or any securities industry self-regulatory organization, responsible for the regulation or supervision of financial institutions." [264]

The Commission requests comment on the following specific issues. Are there specific provisions in proposed Rule 822(c) that should be eliminated or refined? If so, please explain your reasoning. What is the likely impact of this requirement on the SB swaps market, including the impact on the incentives and behaviors of SB SEFs and the willingness of persons to register as SB SEFs?

XX. Core Principle 14—Chief Compliance Officer

Section 3D(d)(14) of the Exchange Act (Core Principle 14), requires registered SB SEFs to designate a CCO and requires the CCO to perform certain duties and to file compliance reports and financial reports annually.[265] Proposed Rule 823 would incorporate the requirements of Core Principle 14 and provide certain additional requirements for its implementation.

A. Appointment and Duties of CCO

Proposed Rule 823(a) would require a registered SB SEF to identify on its Form SB SEF a person who has been designated by the Board to serve as the CCO. The compensation and removal of the CCO would require the approval of a majority of the Board.[266] Proposed Rule 823(b) would incorporate the duties of the CCO contained in Core Principle 14.[267] Specifically, proposed Rule 823(b) would provide that each CCO shall: (1) Report directly to the Board or the senior officer of the SB SEF; (2) review the compliance of the SB SEF with respect to the Core Principles in Section 3D of the Exchange Act and the rules and regulations thereunder; (3) in consultation with the Board or the senior officer, resolve any conflicts of interest that may arise; (4) be responsible for establishing each policy and procedure that is required to be established under Section 3D of the Exchange Act and the rules and regulations thereunder; (5) monitor compliance with the Exchange Act and the rules and regulations thereunder relating to its business as a SB SEF, including each rule prescribed by the Commission under Section 3D of the Exchange Act; (6) establish procedures for the remediation of noncompliance issues identified by the CCO through any (i) compliance office review, (ii) look-back, (iii) internal or external audit finding, (iv) self-reported error, or (v) validated complaint; and (7) establish and follow appropriate procedures for the handling, management response, remediation, retesting, and closing of noncompliance issues.

The CCO would be responsible for, among other things, keeping the SB SEF's Board or senior officer apprised of significant compliance issues and advising of needed changes in the SB SEF's policies and procedures. Given the critical role that a CCO is intended to play in ensuring a SB SEF's compliance with the Exchange Act and the rules and regulations thereunder, the Commission believes that a SB SEF's CCO should be competent and knowledgeable regarding the Federal securities laws and should be empowered with full responsibility and authority to develop and enforce appropriate policies and procedures for the SB SEF.[268] To meet the statutory obligations, a CCO also should have a position of sufficient seniority and authority within the SB SEF to compel others to adhere to the SB SEF's policies and procedures. The Commission notes, however, that the SB SEF would not be required to hire an additional person to serve as its CCO. Instead, the SB SEF could designate an individual already employed by the SB SEF to serve as its CCO.

The Commission is concerned that a SB SEF's commercial interests might discourage its CCO from making forthright disclosure to the Board or the senior officer about any compliance failures. To mitigate this potential conflict of interest, the Commission believes that the CCO should be independent from the SB SEF's management so as not to be conflicted in reporting or addressing any compliance failures. To support this independence, the proposed rule would allow only a majority of the Board to approve the CCO's compensation and to remove the CCO from his or her responsibilities.

The Commission notes that proposed Regulation MC would require a SB SEF to establish a fully independent ROC, which would be the Board committee that would be responsible for monitoring a SB SEF's regulatory program for sufficiency, effectiveness, and independence.[269] The Board of a SB SEF should consider the appropriate reporting structure for the CCO, taking into account the potential conflicts of interest between the CCO and other senior officers of the SB SEF. Because the SB SEF would be required to have a ROC, the Board could elect to delegate to the ROC the duty of overseeing the CCO.

The Commission generally requests comments on all aspects of the proposed rules relating to the appointment and duties of the CCO. Should the Commission require a CCO to meet minimum competency standards? If so, what background, skills and other qualifications should a CCO be required to have? Does the proposed requirement that the CCO report directly to the Board or the senior officer balance the CCO's needs to work effectively with management and to have an adequate separation of business and regulatory influence? Are there situations when the CCO's ability to conduct his or her duties under the Exchange Act could be compromised if he or she were required to report to the senior officer? If so, are there steps that the SB SEF could take to resolve differences between the CCO and the senior officer? Should the Commission require a CCO to report to a specific senior officer? If so, to whom and why? Would it be preferable for the CCO to report to the Board? If so, would it be preferable for the Board to delegate the responsibility for oversight of the CCO to its ROC?

Is the Commission's proposed requirement regarding the Board's approval of a CCO's compensation and removal necessary or appropriate? Absent specific requirements imposed by Federal statute or rules, in general, the entity has the discretion to create the governance structure that it believes best promotes compliance with applicable laws and regulations, in accordance with the relevant laws of the entity's jurisdiction of incorporation or formation. As noted above, the Commission has identified potential conflict concerns between a SB SEF's commercial interests and its regulatory obligations. To mitigate such concerns

[264] 17 CFR 200.80(b)(8).

[265] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(14) of the Exchange Act).

[266] *See* proposed Rule 823(a).

[267] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(14)(B) of the Exchange Act).

[268] The Commission believes that the person that is designated by the Board to serve as the CCO should have the background and qualifications necessary to fulfill the responsibilities of the position.

[269] *See* Regulation MC Proposing Release, *supra* note 82, (proposing that the SB SEF establish a ROC composed solely of independent directors).

and support the independence of the CCO from management of the SB SEF, the Commission is proposing the requirement described above.[270] Do commenters believe that it would be appropriate to impose this requirement, or do commenters believe that SB SEFs would be able to comply with their regulatory obligations without this requirement? Would the removal of this requirement affect the ability of a CCO to comply with the extensive duties required of the CCO under the Dodd-Frank Act? If commenters do not agree that the proposed requirements are necessary or appropriate, why and what would be a better alternative, if any, to promote the independence and effectiveness of the CCO? For example, should the required percentage of Board approval be lower or higher? Or, should the Commission require that the CCO meet separately with the independent directors of the SB SEF, without anyone else present? [271] Would such a requirement promote the independence and effectiveness of the CCO by supporting his or her ability to speak freely with the independent directors about any sensitive compliance issues of concern to any of them? Do commenters believe that it would be appropriate to impose this type of requirement, or do commenters believe that SB SEFs would be able to comply with their regulatory obligations without a requirement such as this?

Should the Commission add a rule explicitly prohibiting any officers, directors, or employees of a SB SEF from, directly or indirectly, taking any action to coerce, manipulate, mislead, or fraudulently influence the CCO in the performance of his other responsibilities?

Are there any terms in proposed Rule 823(b) regarding the duties of the CCO that should be clarified or modified (*e.g.*, "look-back," "self-reported error," or "validated complaint")? If so, which terms and how should they be defined?

Are the duties of the CCO in proposed Rule 823(b) sufficiently clear? Should the Commission provide further guidance or rules on how the CCO should comply with these duties? If so, what kinds of guidance or rules would be appropriate to adopt in this context?

Should the Commission provide guidance in its proposed rules about the CCO's procedures for the remediation of noncompliance issues? Should the Commission provide guidance in its proposed rules on what would be considered "appropriate procedures" for the handling, management response, remediation, retesting, and closing of noncompliance issues? If so, what factors should the Commission take into consideration?

Would the CCO have difficulty discharging any of the obligations under proposed Rule 823? Would any of the CCO's obligations under proposed Rule 823 conflict with current obligations imposed on a CCO? If so, which ones and why? Should the Commission impose any additional duties on the CCO that are not already enumerated in Section 3D(d)(14) of the Exchange Act and incorporated in the proposed rule?

What is the likely impact of the Commission's proposed rule on the SB swap market? Would the proposed rule potentially promote or impede the establishment of SB SEFs? With respect to entities that currently provide a marketplace for trading SB swaps and that may be required to register under the Dodd-Frank Act, how do current practices compare to the practices that the Commission proposes to require in this rule? What are the incremental costs to potential SB SEFs in connection with adding to or revising their current practices in order to implement the Commission's proposed rule?

How might the evolution of the SB swaps market over time affect SB SEFs and impact the Commission's proposed rule?

B. Annual Reports

Section 3D(d)(14)(C) of the Exchange Act requires the CCO to prepare and sign an annual report, in accordance with rules prescribed by the Commission.[272] Proposed Rule 823(c) would prescribe the rules to implement this statutory provision.[273] Proposed Rule 823(c)(1) would implement the requirements in Section 3D(d)(14)(C)(i) under Exchange Act for the CCO to annually prepare and sign a report that contains a description of: (i) The compliance of the SB SEF with respect to the Exchange Act and the rules and regulations thereunder; and (ii) the policies and procedures of the SB SEF (including the code of ethics and conflicts of interest policies of the SB SEF).[274]

The Commission also is proposing certain minimum requirements in proposed Rule 823(c)(1) for the information that should be provided in the CCO's annual report.[275] The proposed minimum requirements would provide guidance for including in the report certain key disclosures about the SB SEF's compliance with the Core Principles. However, this proposed provision is not intended to be an exhaustive list; any other relevant descriptions of the SB SEF's compliance with the Exchange Act and the policies and procedures of the SB SEF related thereto, consistent with the broader statutory requirement in Section 3D(d)(14)(C) of the Exchange Act, also should be included in the CCO's annual report.[276]

Proposed Rule 823(c)(1)(i) through (ii) would require the annual report to include a description of the SB SEF's enforcement of its policies and procedures and information on all investigations, inspections, examinations, and disciplinary cases opened, closed, and pending during the reporting period. Proposed Rule 823(c)(1)(iii) would require the annual report to include a description of all grants of access (including, for all participants, the reasons for granting such access) and all denials or limitations of access (including, for each applicant, the reasons for denying or limiting access), consistent with Rule 811(b)(3). The disclosures in proposed Rule 823(c)(i) through (iii) would provide a basis for evaluating the effectiveness of the SB SEF's compliance program under the standards in Core Principle 2, which generally requires the SB SEF to establish and enforce compliance with its rules.

Proposed Rule 823(c)(1)(iv) through (v) would require the annual report to include any material changes to the SB SEF's policies and procedures since the date of the preceding compliance report and any recommendation for material changes to the policies and procedures as a result of the annual review (including the rationale for such recommendation, and whether such policies and procedures were or will be modified by the SB SEF to incorporate such recommendation).[277] The

[270] The Commission proposed this same requirement in its proposal relating to the registration and regulation of security-based swap data repositories. *See* SDR Release, *supra* note 6.

[271] The concept of an individual with regulatory oversight responsibilities having mandated access to the independent directors without the presence of non-independent directors on the entity's board is not novel, although it has not to date been specifically mandated by the Exchange Act or rules thereunder. *See, e.g.*, Article IV, Sec. 7 of the Nasdaq Bylaws (requiring the Chief Regulatory Officer of Nasdaq to meet in executive session with the Regulatory Oversight Committee of Nasdaq, which is a fully independent committee of the Nasdaq board).

[272] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(14)(C) of the Exchange Act).

[273] *See* proposed Rule 823(c).

[274] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(14)(C)(i) of the Exchange Act) and proposed Rule 823(c)(1).

[275] *See* proposed Rule 823(c)(1).

[276] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(14)(C) of the Exchange Act).

[277] The term "material change" would be defined as a change that a CCO would reasonably need to

proposed requirements should demonstrate the kinds of compliance issues the SB SEF is facing and how the CCO is addressing those issues.

Proposed Rule 823(c)(1)(vi) through (vii) would require the annual report to include the results of the SB SEF's surveillance program (including information on the number of reports and alerts generated, and the reports and alerts that were referred for further investigation or for an enforcement proceeding) and any complaints received on the SB SEF's surveillance program. The proposed requirements should provide a demonstration of the effectiveness of the SB SEF's compliance program in detecting violations and the appropriateness of the SB SEF's response in addressing such detected violations.

Finally, proposed Rule 823(c)(1)(viii) would require the CCO's annual report to include any material compliance matters identified since the date of the preceding compliance report.[278] This proposed requirement would indicate the most significant compliance matters that the SB SEF is dealing with on its market. The Commission notes that individual compliance matters may not be material when viewed in isolation, but may collectively suggest a material compliance matter.

Although the proposed rule would require only annual reviews, the CCO should consider the need for interim reviews in response to significant compliance events, changes in business arrangements, and regulatory developments. For example, if there is an organizational restructuring of a SB SEF, its CCO should evaluate whether the SB SEF's policies and procedures are adequate to guard against potential conflicts of interest. Additionally, if a new rule regarding SB SEFs is adopted by the Commission, then the CCO should review its policies and procedures to ensure compliance with the rule.

Proposed Rule 823(c)(2) would implement the requirement in Section 3D(d)(14)(C)(ii)(I) of the Exchange Act for the CCO to submit the annual report with the appropriate financial reports of the SB SEF at the time of filing.[279] The proposed rule also would implement the requirement in Section 3D(d)(14)(C)(ii)(II) of the Exchange Act that the CCO include a certification in its report, under penalty of law, that the report is accurate and complete.[280]

Under proposed Rule 823(d), the CCO would be required to submit the annual compliance report to the Board for its review prior to the submission of the report to the Commission.[281] The Commission notes, however, that the CCO should promptly bring serious compliance issues to the attention of the full Board or the Board's independent directors rather than wait until an annual report is prepared.

The Commission generally requests comments on all aspects of the proposed rules regarding annual compliance reports. Are the Commission's proposed rules regarding annual compliance reports appropriate and sufficiently clear? If not, why not and what would be a better approach?

Are the proposed definitions of "material change" and "material compliance matter" appropriate? If not, are they over-inclusive or under-inclusive, and how else should these terms be defined?

Proposed Rule 823(c)(1) lists specific disclosures that would need to be included in each annual compliance report. Are there other specific items that should be required? For example, should disclosures about instances when the SB SEF or the Board has not accepted the recommendations of the swap review committee be required to be included in the annual compliance report? Would such information be helpful to the Commission in evaluating whether conflicts of interest are impacting decisions about whether to trade, or how to trade, a particular SB swap?

Should the Commission propose a timeframe for the CCO to submit his or her annual compliance report for the review by the Board? If so, what would be an appropriate timeframe? Should the Commission permit the SB SEF to request an extension to file an annual compliance report (*e.g.,* due to substantial, undue hardship)?

If a CCO reports to the senior officer of the SB SEF rather than to the Board, should the Commission permit the CCO to submit his or her annual compliance report for prior review to the senior officer rather than to the Board, in addition to the Board, or only when the SB SEF does not have a Board? Would any of these alternatives lessen the independence of the CCO in any way?

Should the Commission prohibit a SB SEF's Board from requiring its CCO to make any changes to the annual compliance report? If the Commission permits the CCO to submit his or her annual compliance report to the senior officer for prior review, instead of to the Board or in addition to the Board, should a similar prohibition be applied to the senior officer? Would such a prohibition be necessary, in either case, in light of the CCO's statutory requirement to certify that the compliance report is accurate and complete?

Is the Commission's proposed requirement that the CCO meet separately with the independent directors of a SB SEF appropriate? If not, why not and what would be a better alternative?

Are the Commission's proposed minimum disclosure requirements in the CCO's annual compliance report appropriate? If not, why not and what would be a better alternative? Should the Commission require any other disclosures in the CCO's annual compliance report?

Would keeping the compliance reports confidential encourage the CCO to be more forthcoming about sensitive compliance issues or would it likely not have any impact on the disclosure of such issues? Are there any disadvantages to keeping the CCO's compliance report confidential? How could the Commission address any such disadvantage? Would making the CCO's compliance report public be useful to the public or other regulators?

What is the likely impact of the Commission's proposed rule on the SB swap market? Would the proposed rule potentially promote or impede the establishment of SB SEFs? With respect to entities that currently provide a marketplace for trading SB swaps and that may be required to register under the Exchange Act, as amended by the Dodd-Frank Act, how do current practices compare to the practices that the Commission proposes to require in this rule? What would be the incremental costs to potential SB SEFs in connection with adding to or revising their current practices in order to implement the Commission's proposed rule?

How might the evolution of the SB swaps market over time affect SB SEFs and impact the Commission's proposed rule?

know in order to oversee compliance of the SB SEF. *See* proposed Rule 800.

[278] The term "material compliance matter" would be defined as any compliance matter that the Board would reasonably need to know to oversee the compliance of the SB SEF and includes, without limitation: (1) A violation of the Federal securities laws by the SB SEF, its officers, directors, employees, or agents; (2) a violation of the policies and procedures of the SB SEF, by the SB SEF, its officers, directors, employees, or agents; or (3) a weakness in the design or implementation of the SB SEF's policies and procedures. *See* proposed Rule 800.

[279] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(14)(C)(ii)(I) of the Exchange Act) and proposed Rule 823(c)(2).

[280] *See* Public Law 111–203, § 763(c) (adding Section 3D(d)(14)(C)(ii)(II) of the Exchange Act) and proposed Rule 823(c)(2).

[281] *See* proposed Rule 823(d).

C. Financial Reports

Section 3D(d)(14)(C)(ii)(I) of the Exchange Act requires a compliance report filed by the CCO to be accompanied by each appropriate financial report of the SB SEF that is required to be furnished to the Commission pursuant to Section 3D of the Exchange Act. The Commission is proposing Rule 823(e), which would set forth the appropriate financial reports that a SB SEF would be required to include with its annual compliance reports.[282] Proposed Rule 823(e)(1) would require the financial reports of the SB SEF to: (1) Be a complete set of financial statements of the SB SEF that are prepared in accordance with U.S. generally accepted accounting principles for the most recent two fiscal years of the SB SEF; (2) be audited in accordance with standards of the Public Company Accounting Oversight Board ("PCAOB") by a public accounting firm that is registered with the PCAOB and is qualified and independent in accordance with Rule 2–01 of Regulation S–X (17 CFR 210.2–01); (3) include a report of the registered public accounting firm that complies with paragraphs (a) through (d) of Rule 2–02 of Regulation S–X (17 CFR 210.2–02); and (iv) include the SB SEF's accounting policies and practices.[283]

Under Proposed Rule 823(e)(1)(v), if the SB SEF's financial statements contain consolidated information of the SB SEF's subsidiaries, then the SB SEF's financial statements also would need to provide condensed financial information, in a financial statement footnote, as to the financial position, changes in financial position and results of operations of the SB SEF, as of the same dates and for the same periods for which audited consolidated financial statements are required.[284] Such financial information would need not be presented in greater detail than is required for condensed statements by Rules 10–01(a)(2), (3), and (4) of Regulation S–X. Detailed footnote disclosure that would normally be included with complete financial statements may be omitted with the exception of disclosures regarding material contingencies, long-term obligations, and guarantees. Descriptions of significant provisions of the SB SEF's long-term obligations, mandatory dividend or redemption requirements of redeemable stocks, and guarantees of the SB SEF would also be required to be provided along with a five-year schedule of maturities of debt. If the material contingencies, long-term obligations, redeemable stock requirements and guarantees of the SB SEF have been separately disclosed in the consolidated statements, then they would not need to be repeated in this schedule.[285] This proposed requirement is substantially similar to Rule 12–04 of Regulation S–X, which pertains to condensed financial information of registrants.[286]

Under proposed Rule 823(e)(2), for SB SEFs with affiliated entities (any subsidiary in which the applicant has, directly or indirectly, a 25% interest and for every entity that has, directly or indirectly, a 25% interest in the applicant), for each affiliated entity, the financial report would also be required to include a complete set of unconsolidated financial statements (in English) for the latest two fiscal years and such footnotes and other disclosures as are necessary to avoid rendering the financial statements misleading.[287] The Commission notes that information on affiliated entities is currently requested for national securities exchanges[288] and is important information for the Commission to obtain because the financial health of affiliated entities could potentially have an impact on the financial condition of the SB SEF.

Proposed Rule 823(e)(4) also would require the financial statements to be provided in XBRL, consistent with Rules 405(a)(1), (a)(3), (b), (c), (d), and (e) of Regulation S–T.[289] Specifically, information in the financial statements would be required to be tagged[290] using XBRL to allow the Commission to assess and analyze effectively the SB SEF's financial and operational condition.

Finally, annual compliance reports and financial reports filed pursuant to proposed Rule 823 would be required to be filed within 60 days after the end of the fiscal year covered by such reports.[291]

The Commission notes that with respect to its other registrants, the Commission has required, at a minimum, the proposed financial information and in some instances, significantly more information.[292] The Commission believes that it would be important to obtain an audited annual financial report covering two years from each registered SB SEF to understand the SB SEF's financial and operational condition, particularly because SB SEFs are intended to play a pivotal role in improving the transparency of the OTC derivatives markets.[293] Among other things, the financial statements could help the Commission evaluate whether a SB SEF has adequate financial resources to comply with its statutory obligations or is having financial difficulties. If a SB SEF ultimately ceases doing business, it could create a significant disruption in the OTC derivatives market. The Commission believes that the financial information that it is seeking pertaining to the affiliates of the SB SEF is relevant and necessary as the financial condition of the affiliates could have an immediate or future impact on the condition of the SB SEF.

The Commission requests comments on all aspects of the proposed rules relating to financial statements. Is the Commission's proposed rule regarding a SB SEF's financial report appropriate and sufficiently clear? If not, why not and what would be a better alternative? Should the Commission permit a financial report by a SB SEF that is a foreign private issuer to be in compliance with International Financial Reporting Standards as an alternative to GAAP? If so, why and what are the costs and benefits to permitting this?

Is the Commission's proposed rule requiring financial reports to cover the most recent two fiscal years of a SB SEF appropriate? If not, should the lookback timeframe be greater (*e.g.,* the most recent three fiscal years) or shorter (*e.g.,* the most recent fiscal year)?

Is the Commission's proposed requirement regarding a SB SEF's condensed financial information appropriate and sufficiently clear? If not, why not and what would be a better alternative?

Is the Commission's proposed 60-day timeframe for a SB SEF to file the annual and financial report appropriate?

[282] The financial statements required by these proposed rules are the same as the requirements for the annual financial statements that would be required to be submitted pursuant to Exhibits F and H of proposed Form SB SEF. *See infra* Section XXII. To avoid submitting duplicative financial statements, the CCO may represent in the annual compliance report that the financial statements required by proposed Rule 823(e) have been submitted to the Commission as part of the annual update of Form SB SEF required by proposed Rule 802(f).

[283] *See* proposed Rule 823(e)(1).

[284] *See* proposed Rule 823(e)(1)(v).

[285] *Id.*

[286] *See* 17 CFR 210.9–06.

[287] *See* proposed Rule 823(e)(2).

[288] *See* Form 1 and instructions thereunder.

[289] *See* 17 CFR 232.405 (imposing content, format, submission and Web site posting requirements for an interactive data file, as defined in Rule 11 of Regulation S–T).

[290] Tagging refers to labeling fields of data electronically so that it can be searched electronically by categories. *See* proposed Rule 800.

[291] *See* proposed Rule 823(f).

[292] *See, e.g.,* Rule 17a–5(d) under the Exchange Act, 17 CFR 240.17a–5(d).

[293] *See* Public Law 111–203, § 763(c) (adding Section 3D of the Exchange Act).

If not, should the timeframe be shorter or longer (*e.g.,* 30 days or 90 days)? Would a SB SEF's financial report be useful to the public or other regulators? If so, explain.

Are the financial report requirements relating to certain affiliates of SB SEFs too broad or overly burdensome? Are there any terms in the Commission's proposed rule regarding a SB SEF's financial report that need to be defined or clarified? If so, which terms?

What is the likely impact of the Commission's proposed rule on the SB swap market? Would the proposed rule potentially promote or impede the establishment of SB SEFs? With respect to entities that currently provide a marketplace for trading SB swaps and that may be required to register under the Dodd-Frank Act, how do current practices compare to the practices that the Commission proposes to require in this rule? What would be the incremental costs to potential SB SEFs in connection with adding to or revising their current practices in order to implement the Commission's proposed rule?

How might the evolution of the SB swaps market over time affect SB SEFs and impact the Commission's proposed rule relating to the CCO?

XXI. Registration of Security-Based Swap Execution Facilities

As stated above, a primary goal of the Dodd-Frank Act is to improve the transparency and oversight of the OTC derivatives market and to guard against systemic risk in the trading of these instruments. A key aim of the legislation is to bring the trading of mandatorily cleared OTC derivatives onto regulated markets. In this regard, the Dodd-Frank Act amends the Exchange Act to add new Section 3D of the Exchange Act.[294] Section 3D(a)(1) of the Exchange Act provides that no person may operate a facility for the trading or processing of SB swaps, unless the facility is registered as a SB SEF or as a national securities exchange.[295] Core Principle 1 for SB SEFs, as set forth in Section 3D(d)(1)(A) of the Exchange Act,[296] provides that, to be registered and maintain its registration as a SB SEF, a SB SEF must comply with the 14 Core Principles governing SB SEFs and any requirement that the Commission may impose by rule or regulation.[297]

The Commission's rules currently provide for registration frameworks for two types of trading venues for securities, namely national securities exchange registration and broker-dealer registration for ATSs. SB SEFs represent an additional category of registered entities under the Exchange Act and the Commission preliminarily believes that it would be appropriate to adopt a registration process for SB SEFs that is similar to the Commission's existing registration framework for national securities exchanges. SB SEFs, like national securities exchanges, have regulatory obligations pursuant to the Exchange Act.[298] Also, pursuant to the Dodd-Frank Act, both national securities exchanges and SB SEFs would be permitted to trade SB swaps, although exchange trading of SB swaps is governed by Section 6 of the Exchange Act[299] and other provisions of the Exchange Act relevant to SROs.[300] The registration process for national securities exchanges is already established, but no process exists for SB SEFs. Thus, the Commission is proposing rules that would require an application registration process for SB SEFs and a form for such application, which would be subject to approval by the Commission.

A. Initial SB SEF Registration

1. Procedures for Registration

Proposed Rule 801(a) provides that an application for the registration of a SB SEF would need to be filed electronically in a tagged data format[301] with the Commission on the new proposed Form SB SEF, in accordance with the instructions contained in the Form SB SEF.[302] Proposed Form SB SEF also would be used by a SB SEF for submitting all amendments to the Form SB SEF.[303] The Commission's proposal contemplates the use of an online filing system through which a SB SEF would be able to file a completed Form SB SEF, which would be available on the Commission's Web site and accessible from any computer with Internet access.[304] Based on the widespread use and availability of the Internet, the Commission believes that filing Form SB SEF in an electronic format would be less burdensome and a more efficient filing process for SB SEFs, the Commission, and the public.

The Commission's proposal requires a Form SB SEF to be filed with the Commission in a tagged data format. As part of the Commission's longstanding efforts to increase transparency and the usefulness of information, the Commission has been implementing data-tagging of information contained in electronic filings to improve the accuracy of financial information and facilitate its analysis.[305] Data becomes

[294] *See* Public Law 111–203, § 763(c) (adding Section 3D of the Exchange Act).

[295] *Id.*

[296] *Id.*

[297] *Id.*

[298] For example, pursuant to Section 3D(d)(2) of the Exchange Act, Public Law 111–203, § 763(c), a SB SEF is required to: (1) Establish and enforce compliance with any rule established by it, including (i) the terms and conditions of the SB swaps traded or processed on or through the facility and (ii) any limitation on access to the facility; (2) establish and enforce trading, trade processing, and participation rules that will deter abuses and have the capacity to detect, investigate, and enforce those rules, including means (i) to provide market participants with impartial access to the market; and (ii) to capture information that may be used in establishing whether rule violations have occurred; and (3) establish rules governing the operation of the facility, including rules specifying trading procedures to be used in entering and executing orders traded or posted on the facility, including block trades.

[299] 15 U.S.C. 78f.

[300] *See, e.g.,* Section 19 of the Exchange Act, 15 U.S.C. 78s.

[301] Proposed Rule 800 would define the term "tag" or "tagged" to mean an identifier that highlights specific information submitted to the Commission and that is in the format required by the EDGAR Filer Manual, as described in Rule 301 of Regulation S–T, 17 CRF 232.301.

[302] *See* proposed Rule 801(a).

[303] *See* Section XXI.B *infra* for a discussion of the amendments to Form SB SEF required in proposed Rule 802. An application for registration or any amendment thereto filed pursuant to Regulation SB SEF would be considered a "report" filed with the Commission for purposes of Sections 18(a) and 32(a) of the Exchange Act and the rules and regulations thereunder. *See* proposed Rule 801(f). Exchange Act Sections 18(a) and 32(a) set forth the potential liability for a person who makes, or causes to be made, any false or misleading statement in any "report" filed with the Commission (*e.g.,* Form SDR). Specifically, Exchange Act Section 18(a) provides, in part, that "[a]ny person who shall make or cause to be made any statement in any * * * report * * * which statement was at the time and in the light of the circumstances under which it was made false or misleading with respect to any material fact, shall be liable to any person (not knowing that such statement was false or misleading) who, in reliance upon such statement, shall have purchased or sold a security at a price which was affected by such statement, for damages caused by such reliance, unless the person sued shall prove that he acted in good faith and had no knowledge that such statement was false or misleading." 15 U.S.C. 78r(a). Exchange Act Section 32(a) provides, in part, that "[a]ny person who willfully and knowingly makes, or causes to be made, any statement in any * * * report * * * which statement was false or misleading with respect to any material fact, shall upon conviction be fined not more than $5,000,000, or imprisoned not more than 20 years, or both, except that when such person is a person other than a natural person, a fine not exceeding $25,000,000 may be imposed." 15 U.S.C. 78ff(a).

[304] If the Commission adopts the rule as proposed, it is possible that SB SEFs may be required to file Form SB SEF in paper until such time as an electronic filing system is operational and capable of receiving the form. In such a case, SB SEFs would be notified as soon as the electronic system is operational to accept filings on Form SB SEF.

[305] *See* Regulation S–T, 17 CFR 232. *See also* Securities Act Release No. 8891 (Feb. 6, 2008), 73 FR 10592 (Feb. 27, 2008); Securities Act Release No. 9002 (Jan. 30, 2009), 74 FR 6776 (Feb. 10, 2009); Securities Act Release No. 9006 (Feb. 11, 2009), 74 FR 7748 (Feb. 19, 2009); Exchange Act Release No. 61050 (Nov. 23, 2009), 74 FR 63832 (Dec. 4, 2009);

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machine-readable when it is labeled, or tagged, using a computer markup language that can be processed by software programs for analysis. Such computer markup languages use standard sets of definitions, or "taxonomies," that translate text-based information in Commission filings into structured data that can be retrieved, searched, and analyzed through automated means. Requiring the information to be tagged in a machine-readable format using a data standard that is freely available, consistent, and compatible with the tagged data formats already in use for Commission filings would enable the Commission to review and analyze effectively Form SB SEF submissions.

Proposed Rule 801(a) provides that a registration application on Form SB SEF must include information sufficient to demonstrate compliance with the Exchange Act and rules and regulations thereunder. The proposed rule provides that if a registration application is not complete, the Commission will notify the applicant that the application will not be deemed to have been submitted for purposes of the Commission's review.[306] Pursuant to the proposed rule, an application on Form SB SEF would not be considered to be complete unless an applicant has submitted, at a minimum, the Execution Page and Exhibits as required in proposed Form SB SEF, and any other material that the Commission may require, upon request, in order to be able to determine whether the applicant is able to comply with the Exchange Act and rules and regulations thereunder. Such other material may include, but is not limited to, information regarding the applicant's system test procedures, contingency or disaster recovery plans, and the manner in which the applicant would conduct market and financial surveillance.

Proposed Rule 801(b) sets forth the SB SEF registration application processes for (i) applications received during the initial implementation phase of Regulation SB SEF, from the date of Regulation SB SEF's effectiveness up to and including July 31, 2014 ("initial implementation period"), and (ii) applications received after the initial implementation period (*i.e.,* after July 31, 2014).

Proposed Rule 801(b)(1) would provide that for applications for registration as a SB SEF filed on Form SB SEF with the Commission on or before July 31, 2014, within 360 days of the date of the filing of such application (or within such longer period as to which the applicant consents), the Commission would be required to either grant the registration or institute proceedings to determine whether registration should be denied. Such proceedings would include notice of the grounds for denial under consideration and opportunity for hearing and would be required to be concluded within 450 days after the date on which the application for registration is furnished to the Commission. At the conclusion of such proceedings, the Commission, by order, would be required to grant or deny such registration. The Commission would be able to extend the time for conclusion of such proceedings for up to 90 days if it finds good cause for such extension and publishes its reasons for so finding or for such longer period as to which the applicant consents.

Proposed Rule 801(b)(2) would provide that for applications for registration as a SB SEF filed on Form SB SEF with the Commission after July 31, 2014, within 180 days of the date of filing of such application (or within such longer period as to which the applicant consents), the Commission would be required to either grant the registration or institute proceedings to determine whether registration should be denied. Such proceedings would include notice of the grounds for denial under consideration and opportunity for hearing and would be required to be concluded within 270 days after the date on which the application for registration is furnished to the Commission. At the conclusion of such proceedings, the Commission, by order, would be required to grant or deny such registration. The Commission would be able to extend the time for conclusion of such proceedings for up to 90 days if it finds good cause for such extension and publishes its reasons for so finding or for such longer period as to which the applicant consents.

The proposed rule further provides that the Commission would grant the registration of an applicant if it finds that the requirements of the Exchange Act and the rules and regulations thereunder with respect to the applicant are satisfied, and would deny such registration if it does not make such finding.[307]

The proposed process for SB SEF's to apply for initial registration would provide a mechanism for an applicant to demonstrate that it has the operational and financial capability to operate as a SB SEF and can comply with the Federal securities laws and the rules and regulations thereunder, including the Core Principles, and would allow the Commission to consider the materials provided by the SB SEF and to make an informed determination as to whether the SB SEF complies with the Exchange Act and the rules and regulations thereunder. In addition, the application process would allow the Commission staff to ask questions and, as needed, to require amendments or changes to the application or additional information to address legal and regulatory concerns before approving an application for registration. Further, providing a process and timeframes for the application process would provide certainty to applicants as to the procedural aspects of registering as a SB SEF.

As no SB SEF is currently registered with the Commission and a number of entities have informed the Commission that they may seek to register as a SB SEF, the Commission contemplates receiving a large volume of applications for registration as a SB SEF within the first 3 years following any adoption of rules applicable to SB SEFs. The proposed timeframes for the Commission to review applications for registration as a SB SEF set forth in proposed Rule 801(b) recognize that, as the Commission has limited resources, the Commission may require an extended period of time to review these applications. For applications filed after the initial implementation period, the proposed timeframes for the Commission to review applications for registration as a SB SEF would be decreased to mirror those set forth in Section 19(a)(1) of the Exchange Act applicable to the review of SRO registration applications. The Commission believes that the timeframes for Commission review during and after the initial implementation period are appropriate in light of the anticipated volume of registration applications during the initial implementation period. The Commission also believes that the temporary registration provisions of proposed Rule 801(c), discussed below, should work in combination with the proposed review and approval process to allow both the Commission and entities seeking to register as SB SEFs to comply with the provisions of the Exchange Act, as amended by the Dodd-Frank Act, in a timely manner. In addition, the Commission notes that the process for the Commission to review registration applications for SB SEFs would be similar to the process for reviewing applications of other registrants by the Commission (*e.g.,* national securities exchanges, national

Investment Company Release No. 29132 (Feb. 23, 2010), 75 FR 10060 (Mar. 4, 2010).

[306] *See* Proposed Rule 801(a).

[307] *See* proposed Rule 801(b)(3).

securities associations, and clearing agencies).[308]

The Commission requests comments on all aspects of the proposed rules relating to the registration process for SB SEFs. Is the Commission's proposed registration process appropriate and sufficiently clear? If not, why not and what would be a better alternative? Are the timeframes in the proposed registration process appropriate? If not, why not and what would be more appropriate timeframes? Should timeframes be omitted from the process? Should different time periods apply to the Commission's review of applications during the initial implementation period? If not, why not? Should the Commission have greater flexibility to extend the timeframes?

Are the proposed factors in determining whether the Commission should grant or deny an application for registration appropriate and sufficiently clear? If not, why not? Should the Commission take into consideration any other factors in determining whether to grant or deny an application for registration?

In order to form a more complete and informed basis on which to determine whether to grant, deny, or revoke a SB SEF's registration, the Commission is considering whether to adopt a requirement that a SB SEF file with the Commission, as a condition of registration or continued registration, a review relating to the SB SEF's operational capacity and ability to meet its regulatory obligations. The Commission could require such a review to be in the form of a report conducted by the SB SEF, an independent third party, or both. This review could be required as an exhibit to Form SB SEF at the time of registration or as an amendment to Form SB SEF at a later date (*e.g.,* one year after the registration becomes effective) to allow the review to evaluate the SB SEF's capabilities after some operational experience following registration.

Should the Commission require a SB SEF to conduct or obtain a review relating to the SB SEF's operational capacity and ability to meet its regulatory obligations? If not, why not? If so, how should the Commission define the nature and scope of this review? Should the Commission identify a specific framework for SB SEFs or independent third parties to follow when conducting a review? If so, what would the critical components of the framework include? Are existing frameworks available that are suitable for this purpose and, if so, which ones would be considered appropriate? Should the review resemble a report, audit, or something else?

Should the Commission require the SB SEF, an independent third party, or some other entity to conduct the review? What are examples of such a review? Should the Commission require a review on a case-by-case basis or for all SB SEFs? Should the Commission require that the review be filed with the Commission? If not, why not? If so, should it be required to be filed with the Commission as a condition of registration pursuant to proposed Rule 801? If not, why not? When should the Commission require the filing of any review? Would conducting or obtaining a review, or filing such review with the Commission, impose impracticable burdens and costs on SB SEFs? Please explain the burdens and quantify the costs of such a review.

If the Commission were to adopt a rule requiring a review by an independent third party, should the rule specify some minimum standard of review or the types of review that should be performed? If so, what should the standards be? Should there be minimum qualification standards for the independent third party? Are there any particular types of third party service providers that should not be permitted to conduct a review of a SB SEF? Should the Commission also require that a SB SEF certify the accuracy of the review and provide disclosure regarding the nature of the review, findings, and conclusions? To what extent should a SB SEF be permitted to rely on a third party that it hired to perform the review? Should the Commission condition the ability of a SB SEF to rely on a third party's review? Would a review by an independent third party be necessary in light of the CCO's annual compliance report or proposed Rule 822?

2. Temporary Registration

Proposed Rule 801(c) under Regulation SB SEF would provide a method for the Commission to grant temporary registration to SB SEFs.[309] Specifically, for any application for registration as a SB SEF filed with the Commission in accordance with the provisions of proposed Rule 801(a) on or before July 31, 2014 for which the SB SEF indicates on the Execution Page that it would like to be considered for temporary registration, the Commission could grant such temporary registration to the SB SEF, which temporary registration would expire on the earlier of: (1) The date that the Commission grants or denies registration of the SB SEF; or (2) the date that the Commission rescinds the temporary registration of the SB SEF. In considering whether to grant a request for temporary registration, the Commission would review and consider the information and materials provided by the SB SEF in its registration application on Form SB SEF that the Commission believes to be relevant, including, but not limited to: Whether the applicant's trading system satisfies the definition of a "security-based swap execution facility" in Section 3(a)(77) of the Exchange Act and any Commission rules, interpretations or guidelines regarding such definition;[310] any access requirements or limitations imposed by the SB SEF;[311] the ownership and voting structure of the SB SEF;[312] and any certifications made by the SB SEF, including with respect to its capacity to function as a SB SEF and its compliance with the Exchange Act and the rules and regulations thereunder.[313] In addition, the Commission would expect that SB SEFs registered on a temporary registration basis demonstrate that they have the capacity and resources to comply with their regulatory obligations on an ongoing basis as their business evolves. After granting a temporary registration to a SB SEF, the Commission could rescind such temporary registration if, upon further review, the Commission found that the applicant did not meet the requirements for granting the registration of a SB SEF set forth in proposed Rule 801(b)(3),[314] or if the conditions for revoking or canceling the registration of a SB SEF in proposed Rules 804(d) and (e) under Regulation SB SEF were met.[315]

The Dodd-Frank Act provides that, unless otherwise provided, the provisions of Title VII shall be effective on the later of 360 days after the date

[308] *See* Section 19(a)(1) of the Exchange Act, 15 U.S.C. 78s(a)(1). In addition, the Commission notes that the SEC Rules of Practice would be applicable to the Commission's review of registration applications for SB SEFs. *See* 17 CFR 201.100, *et seq.*

[309] *See* proposed Rule 801(c).

[310] *See* Exhibit I, Item 1 of proposed Form SB SEF.

[311] *See* Exhibit I, Item 2 and Exhibit L of proposed Form SB SEF.

[312] *See* Exhibit E of proposed Form SB SEF.

[313] *See* Execution Page of proposed Form SB SEF.

[314] *See* proposed Rule 801(b)(3).

[315] *See* proposed Rule 804(c) and discussion *infra* Section XXI.C. Proposed Rule 804(c) provides that the Commission may, by order, cancel or revoke a SB SEF's registration if the Commission finds that the SB SEF obtained its registration by making a false or misleading statements with respect to any material fact, is no longer in existence, has ceased to do business in the capacity specified in its application for registration, or has violated or failed to comply with any provision of the Federal securities laws and the rules and regulations thereunder.

of the enactment of Title VII or not less than 60 days after the publication of final rules or regulations implementing such provisions.[316] The Commission preliminarily believes that the proposed temporary registration process for SB SEFs could serve as a useful tool during the initial implementation period to allow the Commission to temporarily register an applicant as a SB SEF following an initial review of a SB SEF's application for registration where it believes such temporary registration is appropriate. The Commission preliminarily believes that this would be beneficial in order to allow SB SEFs to comply with the timeframe set forth in the Dodd-Frank Act while still giving the Commission sufficient time to review an application more thoroughly before granting a registration that is not limited in duration. A SB SEF that is temporarily registered with the Commission would still need to comply with all provisions of the Exchange Act and the rules and regulations thereunder, including Section 3D of the Exchange Act and proposed Regulation SB SEF.

The Commission requests comments on all aspects of the proposed rules with respect to temporary registration. Is the Commission's proposed rule regarding temporary registration appropriate? If not, why not? Is the Commission's proposed rule for temporary registration sufficiently clear? If not, how can it be clarified? What is the best method for a SB SEF to request temporary registration from the Commission? Is it appropriate to include a check box on Form SB SEF as proposed? Would a different method be more appropriate? Are there more appropriate methods other than temporary registration that would allow SB SEFs to meet the timelines for compliance set forth in the Dodd-Frank Act? If so, what are those methods?

As discussed above, the Commission anticipates receiving a large volume of applications for registration as a SB SEF within the first 3 years following the adoption of the proposed rules, and the ability to grant temporary registration during such initial implementation period could be an important tool for the Commission to allow SB SEFs to comply with the provisions of the Exchange Act, as amended by the Dodd-Frank Act, while providing the Commission with additional time to conduct a thorough review of the SB SEF prior to granting permanent registration. Should temporary registration be limited to those registration applications filed during the initial implementation period as proposed? If not, why not? Should the Commission be able to grant temporary registration to any registration application, regardless of when filed? If temporary registration should be limited to a specific time period, would a time period other than the initial implementation period be appropriate? If so, what time period would be appropriate?

Should temporary registration be granted only after the filing of a completed registration application? Should there be a separate application for temporary registration other than proposed Form SB SEF? Should the proposed rule specify the items the Commission must review prior to granting temporary registration? Should temporary registration be granted by the Commission only when certain conditions are met? If so, what should those conditions be? Should the proposed rule specify the findings the Commission must make in order to grant a temporary registration? In what instances should a temporary registration be denied? For example, should a temporary registration be denied if a Form SB SEF is not sufficiently complete? Are there any reasons not specified in this release upon which a temporary registration should be rescinded?

Should the Commission be required to grant temporary registration within a specified time frame? If so, what time period would be appropriate? Is it appropriate to stay the time period for Commission action on a registration application if the Commission grants a SB SEF temporary registration? If so, should such stay be limited in duration? What would be the appropriate time period for such stay?

Would it be feasible for a SB SEF to comply with Section 3D of the Exchange Act and the rules and regulations thereunder within 60 days after publication of the final rules applicable to SB SEFs? If not, which requirement(s) would be difficult for a SB SEF to comply with upon the effective date? Should any requirement(s) be imposed on an incremental basis or with a phased-in approach? If so, what would be an appropriate timeframe for such requirement(s) to be met?[317]

Is it essential that a SB SEF that is temporarily registered be required to comply with all provisions of the Exchange Act and the rules and regulations thereunder? If not, are there specific requirements that the Commission should consider not requiring a SB SEF to comply with during a temporary registration period? If so, what are such requirements and for what reasons should the Commission consider not requiring them?

3. Non-Resident Persons and Control Persons

Proposed Rule 801(d) would require each SB SEF applying for registration with the Commission to designate and authorize on Form SB SEF an agent in the United States, other than a Commission member, official, or employee, to accept notice or service of process, pleadings, or other documents in any action or proceedings brought against the SB SEF to enforce the Federal securities laws and the rules and regulations thereunder.[318]

The Commission preliminarily believes that before granting registration to a SB SEF, it is appropriate to obtain assurance that such person has an agent for service of process in the United States in order to facilitate proper notification to the SB SEF of any actions or proceedings the Commission may wish to bring against such SB SEF.

Proposed Rule 801(e) would require any person applying for registration on Form SB SEF that is controlled by another person[319] to certify on Form SB SEF and provide an opinion of counsel that any person that controls such applicant will consent to and can, as a matter of law, (1) provide the Commission with prompt access to its books and records, to the extent such books and records are related to the activities of the SB SEF; and (2) submit to onsite inspection and examination by representatives of the Commission with respect to the activities of the SB SEF.[320] In addition, proposed Rule 802(c) would require any SB SEF controlled by any other person to file an amendment to Exhibit P on Form SB SEF within 5 business days after any changes in the legal or regulatory framework of any person that controls

[316] *See* Public Law 111–203, § 774.

[317] *See infra* Section XXV for a discussion regarding a potential phased-in approach.

[318] *See* proposed Rule 801(d).

[319] For purposes of Regulation SB SEF, proposed Rule 800 would define the term "control" or any derivatives thereof as the direct or indirect possession of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise. Proposed Rule 800 would provide that a person would be presumed to control another person if the person: (1) Is a director, general partner, or officer exercising executive responsibility (or having similar status or functions); (2) directly or indirectly has the right to vote 25% or more of a class of voting securities or has the power to sell or direct the sale of 25% or more of a class of voting securities; or (3) in the case of a partnership, has the right to receive, upon dissolution, or has contributed, 25% or more of the capital. *See* Instructions to Form 1.

[320] *See* proposed Rule 801(e).

the SB SEF that would impact the ability of or the manner in which any such person consents to or provides the Commission prompt access to its books and records, to the extent such books and records are related to the activities of the SB SEF, or impacts the Commission's ability to inspect and examine any such person with respect to the activities of the SB SEF.[321] Such amendment would be required to include a revised opinion of counsel pursuant to Exhibit P describing how, as a matter of law, any person that controls the SB SEF would continue to meet its obligations to consent to and provide the Commission with prompt access to its books and records, to the extent such books and records are related to the activities of the SB SEF, and to consent to and be subject to onsite inspection and examination by representatives of the Commission with respect to the activities of the SB SEF under such new legal or regulatory framework.[322] The Commission emphasizes that the proposed provisions would be applicable only to those books and records or activities that are related to the activities of the SB SEF. The Commission believes that it is important for the SB SEF to have access to books and records that are related to the activities of a SB SEF and to have examination and inspection authority with respect to activities of a SB SEF, in order for a SB SEF to be able to effectively carry out its regulatory responsibilities. Similarly, the Commission believes that it is important for the Commission to have access to those books and records and such examination and inspection authority so that it may effectively conduct its oversight and regulatory responsibilities under the Exchange Act.

Proposed Rule 801(f) would require that any non-resident person [323] seeking to register as a SB SEF certify on Form SB SEF and provide an opinion of counsel that the SB SEF can, as a matter of law, (1) provide the Commission with prompt access to the books and records of such SB SEF and (2) submit to onsite inspection and examination by representatives of the Commission.[324]

The Commission preliminarily believes that before granting registration to a non-resident SB SEF, it is appropriate to obtain assurance that such person is legally permitted to provide the Commission with prompt access to its books and records and to be subject to inspection and examination by the Commission. Similarly, the Commission preliminarily believes that before granting registration to a SB SEF controlled by another person, it is appropriate to obtain assurance that the person controlling such SB SEF is legally permitted to provide the Commission with prompt access to its books and records related to the SB SEF and to be subject to inspection and examination by the Commission with respect to activities of the SB SEF. The Commission preliminarily believes that the certifications and opinions of counsel required by proposed Rules 801(e) and (f) would be important to confirm that each non-resident SB SEF or control person of a SB SEF has taken the necessary steps to be in the position to provide the Commission with prompt access to its books and records and to be subject to inspection and examination by the Commission. Certain foreign jurisdictions may have laws that complicate the ability of financial institutions, such as SB SEFs located in their jurisdictions, from sharing or transferring certain information, including personal financial data of individuals that financial institutions come to possess from third parties (*i.e.,* personal data relating to the identity of market participants or their customers). Providing an opinion of counsel that the SB SEF can provide prompt access to books and records and can be subject to inspection and examination would allow the Commission to better evaluate a SB SEF's ability to meet the requirements of registration and ongoing supervision. In addition, certain persons controlling a SB SEF may not be under the jurisdiction of the Commission or may be non-resident persons. Providing an opinion of counsel that such control persons have consented to and can provide prompt access to books and records and be subject to inspection and examination would help the Commission to monitor and oversee individuals that control SB SEFs in cases where such individuals may not otherwise subject to the jurisdiction of the Commission or may be subject to foreign jurisdictions. Failure to make these certifications or provide an opinion of counsel may be a basis for the Commission to deny an application for registration. Similarly, if a registered non-resident SB SEF or a registered SB SEF that is controlled by another person becomes unable to comply with these certifications or provide such opinions of counsel, then this may be a basis for the Commission to revoke the SB SEF's registration.[325]

The Commission requests comments on all aspects of the proposed rules relating to non-resident persons and applicants controlled by other persons seeking to register as SB SEFs. Is the Commission's proposed rule regarding service of process appropriate and sufficiently clear? If not, why not and what would be a better alternative? Should the Commission impose any minimum requirements on the agent whom a person designates to accept any notice or request for service of process? Are there any factors that the Commission should take into consideration to help provide effective service of process on a non-resident person or a person controlled by another person applying for registration as a SB SEF?

If a non-resident SB SEF that is registered in a similar capacity in a foreign jurisdiction seeks to apply for registration as a SB SEF with the Commission, should the registration process for the non-resident SB SEF be any different than the Commission's proposed registration process? For example, should the registration process incorporate additional registration requirements for such non-resident SB SEF? Should the Commission consider any other factors relating to a non-resident SB SEF with respect to the Commission's registration rules or in general?

Are there any factors that the Commission should take into consideration to ensure that a non-resident person seeking to register as a SB SEF can, in compliance with applicable foreign laws, provide the Commission with access to its books and records and can submit to inspection and examination by the Commission? Should such a non-resident person be required to provide any additional information or documents on proposed Form SB SEF to establish its ability to comply with the Federal securities laws and the rules and regulations thereunder?

Are there any factors that the Commission should take into consideration to ensure that a person controlling a person seeking to register as a SB SEF can provide the Commission with access to its books

[321] *See* proposed Rule 802(c).

[322] *Id.*

[323] The term "non-resident person" would be defined to mean: (1) In the case of an individual, one who resides in or has his principal place of business in any place not in the United States; (2) in the case of a corporation, one incorporated in or having its principal place of business in any place not in the United States; and (3) in the case of a partnership or other unincorporated organization or association, one having its principal place of business in any place not in the United States. *See* proposed Rule 800.

[324] *See* proposed Rule 801(f).

[325] *See* proposed Rule 804(d) and discussion *infra* Section XXI.C.

and records and can submit to inspection and examination by the Commission? Should such control persons or the SB SEFs which they control be required to provide any additional information or documents on proposed Form SB SEF to establish the ability of the SB SEF to comply with the Federal securities laws and the rules and regulations thereunder? For example, should a SB SEF controlled by another person be required to provide on proposed Form SB SEF a copy of the document evidencing the consent by the controlling person to the books and records and examination and inspections requirements contained in proposed Rule 801(e)?

B. Proposed Filing Requirements for Maintaining SB SEF Registration

Proposed Rule 802 under Regulation SB SEF would require SB SEFs registered with the Commission to submit certain amendments and updates to Form SB SEF. Proposed Rule 803 under Regulation SB SEF would require SB SEFs registered with the Commission to file certain supplemental information with respect to the trading of SB swaps.

Proposed Rule 802(a) would require a SB SEF to file an amendment to its Form SB SEF promptly, but in no event later than five business days, after discovering that any information filed on Form SB SEF, any statement therein, or any exhibit or amendment thereto, was inaccurate when filed in order to correct such inaccuracies.

Proposed Rule 802(b) would require a registered SB SEF to file an amendment on Form SB SEF with the Commission within five business days after any action is taken that renders inaccurate, or that causes to be incomplete, any information filed on the Execution Page of the SB SEF's Form SB SEF, or any amendment thereto, or any information filed as part of Exhibits C, E, G, or N,[326] or any amendments thereto.[327] Any such amendments must set forth the nature and effective date of the action taken, provide any new information, and correct any information rendered inaccurate. Proposed Rule 802(c) would require a SB SEF that is under the control of any other person to file an amendment to Exhibit P to its Form SB SEF within 5 business days after any changes in the legal or regulatory framework of any person that controls the SB SEF that would impact the ability of or the manner in which any such person consents to or provides the Commission prompt access to its books and records, to the extent such books and records are related to the activities of the SB SEF, or impacts the Commission's ability to inspect and examine any such person with respect to the activities of the SB SEF.[328] Such amendment would be required to include a revised opinion of counsel pursuant to Exhibit P describing how, as a matter of law, any person that controls the SB SEF will continue to meet its obligations to consent to and provide the Commission with prompt access to its books and records, to the extent such books and records are related to the activities of the SB SEF, and to consent to and be subject to onsite inspection and examination by representatives of the Commission under such new legal or regulatory framework.[329] Proposed Rule 802(d) would require non-resident SB SEFs to file an amendment to Exhibit P to their Form SB SEF within five business days after any changes in legal or regulatory framework that would impact the SB SEF's ability to or the manner in which it provides the Commission prompt access to its books and records or impacts the Commission's ability to inspect and examine the SB SEF.[330] Such amendment would be required to include a revised opinion of counsel describing how, as a matter of law, the entity will continue to: (1) meet its obligations to provide the Commission with prompt access to its books and records and (2) be subject to onsite inspection and examination by representatives of the Commission under such new legal or regulatory framework.[331]

The Commission preliminarily believes that it is appropriate to require the updating of only the Execution Page and Exhibits C, E, G, and N to proposed Form SB SEF on a continuous basis. The exhibits required to be updated pursuant to proposed Rule 802(b) are substantially similar to the exhibits to Form 1 required to be updated on a continuous basis by national securities exchanges pursuant to Rule 6a–2 under the Exchange Act.[332] The Commission believes that it is important for the Commission to receive updates to the information included in the enumerated exhibits, namely information regarding a SB SEF's governance, ownership, operations, and criteria used to determine the SB swaps that may be traded on the SB SEF, on a real-time basis to allow the Commission to effectively oversee SB SEFs to ensure compliance with the Exchange Act. The Commission also believes that it is important for the Commission to receive updated opinions of counsel under Exhibit P pursuant to proposed Rules 802(c) and (d) to ensure that the Commission can oversee and ensure compliance with the Exchange Act of non-resident SB SEFs and control persons of SB SEFs. Although the comparable amendments to the Form 1 for national securities exchanges are required to be filed within 10 days pursuant to Rule 6a–2, given the improvements in technology since the adoption of Rule 6a–2, the Commission preliminarily believes that five business days should provide SB SEFs sufficient time to prepare and file a Form SB SEF amendment. In addition, the proposed time frame would ensure that the relevant exhibits remain timely and that the Commission has up-to-date information in a timely manner.

Proposed Rule 802(e) also would provide that if the number of changes to be reported in an amendment, or the number of amendments filed, are so great that the purpose of clarity will be promoted by the filing of a new complete Form SB SEF and exhibits, a SB SEF may elect to, or upon request of any representative of the Commission shall, file as an amendment a complete new Form SB SEF together with all exhibits thereto.

Under proposed Rule 802(f), a registered SB SEF would be required to update its Form SB SEF on an annual basis. Specifically, within 60 days of the end of its fiscal year, a registered SB SEF would be required to file an amendment to its Form SB SEF to update the Form SB SEF in its entirety.[333] Each exhibit to the amended Form SB SEF would be required to be up-to-date as of the end of the latest fiscal year of the SB SEF.[334] The purpose of this requirement is to provide the Commission and the public with updated information on all the exhibits required in the Form SB SEF, particularly those exhibits that are not otherwise required to be updated under proposed Rules 802(b), (c) and (d), on an annual basis. The Commission preliminarily believes that a 60-day filing deadline would give SB SEFs sufficient time in which to file an annual amendment to Form SB SEF.

[326] These exhibits pertain to the list of officers, governors and committees of the SB SEF (Exhibit C), ownership of the SB SEF (Exhibit E), certain material operating agreements (Exhibit G), and criteria for determining what securities may be traded (Exhibit N).

[327] *See* proposed Rule 802(b).

[328] *See* proposed Rule 802(c).

[329] *Id.*

[330] *See* proposed Rule 802(d).

[331] *Id.*

[332] 17 CFR 240.6a–2.

[333] *See* proposed Rule 802(f).

[334] *See id.*

Proposed Rule 803 would require a registered SB SEF to file with the Commission any material relating to the trading of SB swaps (including notices, circulars, bulletins, lists, and periodicals) issued or made generally available to SB SEF participants. A SB SEF would be required to file such supplementary material with the Commission upon issuing or making the material available to SB SEF participants.[335] However, if such information is available continuously on an Internet Web site controlled by the SB SEF, the SB SEF may indicate to the Commission the location of the Web site and certify that such information is accurate instead of filing with the Commission.[336]

The Commission preliminarily believes that the amendments required by proposed Rule 802 and the supplemental material required by proposed Rule 803 would provide a useful tool for the Commission to carry out its oversight of SB SEFs and their compliance with the Exchange Act and the rules and regulations thereunder. Requiring SB SEFs to provide consistent and up-to-date disclosures about significant changes in their governance, ownership, operations and criteria used to determine the SB swaps that may be traded on the SB SEF, and requiring non-resident SB SEFs and SB SEFs controlled by another person to update the opinion of counsel whenever changes in legal or regulatory framework would impact their ability to comply with proposed Rules 801(e) and (f), respectively, pursuant to proposed Rules 802(b), (c) and (d) would provide the Commission with important information in monitoring whether a SB SEF is in compliance with the Core Principles throughout its fiscal year. Requiring a SB SEF to update its Form SB SEF and the exhibits thereto on an annual basis pursuant to proposed Rule 802(f) would provide updated information on the parts of the Form SB SEF that are not required to be updated within five business days and thus enable the Commission to have a full picture of the changes at a SB SEF on a year-to-year basis. Requiring SB SEFs to provide to the Commission material made available to SB SEF participants regarding the trading of SB swaps pursuant to proposed Rule 803 would provide the Commission with important information to monitor the trading of SB swaps on the SB SEF and whether such trading is being conducted in compliance with the Federal securities laws and the rules and regulations thereunder.

Providing the Commission with the necessary information it needs to effectively regulate SB SEFs and the trading of SB swaps on SB SEFs is especially important because SB SEFs would be new entities and SB SEFs, and the trading of SB swaps on SB SEFs, would be newly regulated by the Commission. The operation of SB SEFs and trading of SB swaps on SB SEFs is likely to change as the regulated market for SB swaps and the trading of SB swaps on trading venues regulated by the Commission continue to develop. The proposed amendments to Form SB SEF, including the proposed annual update, and the proposed supplemental information filing, would help the Commission keep abreast of the changes that may occur with respect to the trading of SB swaps on SB SEFs, and the operation and ownership of SB SEFs, and thus should enable the Commission to more effectively regulate the trading of SB swaps and SB SEFs.

The Commission requests comments on all aspects of the proposed rules relating to required amendments and updates to proposed Form SB SEF and the required filing of supplemental information. Are the Commission's proposed rules appropriate and sufficiently clear? If not, why not and what would be a better alternative? Are the exhibits to proposed Form SB SEF that would require prompt updating pursuant to proposed Rule 802(b) appropriate? Are there other exhibits to Form SB SEF that should be updated on a continuous basis? Are there exhibits that should not be updated on a continuous basis? Is it appropriate to require SB SEF's to update their registration statement annually? Would a different time period be more appropriate? What would be the cost to SB SEFs of the proposed rules requiring amendments?

Is the material required to be filed pursuant to proposed Rule 803 appropriate? Is there other information that the Commission should require to be filed with respect to the trading of SB swaps? Is there information that the Commission should not request? Should the Commission request any information at all? Is it appropriate, in lieu of requiring a SB SEF to file supplemental material with the Commission pursuant to proposed Rule 803(a), to allow the SB SEF to direct the Commission to a Web site where such information is located and certify that the information is accurate pursuant to proposed Rule 803(b)? Should the Commission make such an allowance for SB SEFs with respect to required amendments pursuant to proposed Rule 802?

C. Withdrawal or Revocation of Registration of SB SEF

Proposed Rule 804 under Regulation SB SEF would permit a registered SB SEF to withdraw from registration by filing a written notice of withdrawal with the Commission, which notice must designate a person associated with the SB SEF to serve as the custodian of the SB SEF's books and records.[337] Prior to filing a notice of withdrawal, a SB SEF would be required to file an amended Form SB SEF to update any inaccurate information.[338] A notice of withdrawal from registration filed by a SB SEF would become effective on the 60th day after the filing thereof with the Commission, or within such longer period of time as to which such SB SEF consents or which the Commission, by order, may determine as necessary or appropriate in the public interest or for the protection of investors, or within such shorter period of time as the Commission may determine.[339]

The Commission preliminarily believes that is appropriate to provide for a mechanism for SB SEFs to withdraw from registration. In addition, the Commission preliminarily believes that 60 days following notice of withdrawal is an appropriate effective date for any SB SEF registration withdrawal. Providing a period between filing of notice of withdrawal and the effective date of any withdrawal should enable the Commission to allow a SB SEF to withdraw its registration with the Commission and cease operating as a SB SEF and market participants to react to any such withdrawal without dislocating the SB swap market or causing any other unintended consequences with respect to the trading of SB swaps.

Proposed Rule 804(d) would provide that the Commission may, by order, revoke the registration of a registered SB SEF if the Commission finds, on the record after notice and opportunity for hearing, that the SB SEF obtained its registration by making false or misleading statements with respect to any material fact or has violated or failed to comply with any provision of the Federal securities laws or the rules

[335] *See* proposed Rule 803(a).

[336] *See* proposed Rule 803(b).

[337] *See* proposed Rule 804(a). A notice of withdrawal filed pursuant to proposed Rule 804 would be considered a "report" filed with the Commission for purposes of Sections 18(a) and 32(a) of the Exchange Act and the rules and regulations thereunder. *See* proposed Rule 804(c). *See also supra* note 303.

[338] *See* proposed Rule 804(a).

[339] *See* proposed Rule 804(b).

and regulations thereunder.[340] Pending a final determination as to whether the registration of a SB SEF shall be revoked, the Commission may, by order, suspend the registration of the SB SEF if such suspension appears to the Commission, after notice and opportunity for hearing, to be necessary or appropriate in the public interest or for the protection of investors.[341] The Commission believes that it is appropriate to provide a mechanism for the Commission to revoke a SB SEF's registration if a SB SEF obtained its registration unlawfully or has violated the Federal securities laws or rules or regulations thereunder.

Proposed Rule 804(e) would provide that the Commission may, by order, cancel the registration of a SB SEF if the Commission finds that the SB SEF is no longer in existence or has ceased to do business in the capacity specified in its application for registration.[342] The Commission believes that it is appropriate to provide a mechanism for the Commission to cancel a SB SEF's registration if a SB SEF is no longer in existence or has ceased to do business in the manner set forth in the registration application.

The Commission requests comments on all aspects of the proposed rule relating to withdrawal or revocation of registration. Is the Commission's proposed rule regarding the withdrawal, revocation and cancellation of a SB SEF's registration appropriate and sufficiently clear? If not, why not and what would be a better alternative? Should a SB SEF be required to file an amendment on Form SB SEF before withdrawing its registration? If not, why not and what would be a better alternative? Should the Commission require a SB SEF to file a form to request withdrawal of registration? If so, why and what should the SB SEF be required to disclose in the form? Should this form be required in lieu of or in addition to an amendment on Form SB SEF? Is the proposed effective date of 60 days from the filing of the notice of withdrawal with the Commission appropriate? If not, would an earlier or later date be more appropriate? Are the findings required by the Commission to revoke, suspend or cancel a SB SEF's registration appropriate? Are any other instances not specified in this proposed rule in which the Commission should revoke, suspend or cancel a SB SEF's registration?

[340] *See* proposed Rule 804(d).

[341] *Id.*

[342] *See* proposed Rule 804(e).

XXII. New Proposed Form SB SEF for the Registration of Security-Based Swap Execution Facilities

The Commission is proposing that applications for registration as a SB SEF, and amendments to such registration, be submitted on new proposed Form SB SEF. Proposed Form SB SEF is similar in style and format to the existing Form 1 for registration as a national securities exchange. Proposed Form SB SEF, however, is tailored to solicit information that the Commission believes would be useful for considering whether a SB SEF meets the requirements for registration in Section 3D of the Exchange Act, including whether the SB SEF can comply with the Core Principles contained in Section 3D(d) of the Exchange Act, and the rules thereunder, including proposed Regulation SB SEF.

The Execution Page to proposed Form SB SEF would require an applicant to provide certain identifying information. The Execution Page would include a box for the applicant to indicate whether the applicant was seeking consideration for temporary registration pursuant to proposed Rule 801(c). In addition, the Execution Page would require the applicant to designate and authorize an individual, other than a Commission official, for service of process, pleadings, or other documents in connection with any action or proceeding against the applicant, as required by proposed Rule 801(d).

The Execution Page to proposed Form SB SEF further would require the applicant to certify that the statements contained therein are current, true and complete, and that the applicant is currently in compliance with, and is currently operating its business in a manner consistent with, the Exchange Act and all rules and regulations thereunder. The applicant also would be required to certify that it is so organized, and has the capacity, to assure the prompt, accurate, and reliable performance of its functions as a SB SEF, and that it has the capacity to fulfill its obligations under all international information-sharing agreements to which it is a party. In addition, the applicant would be required to certify that any person that controls the applicant has consented to and can, as a matter of law, (1) provide the Commission with prompt access to its books and records, to the extent such books and records are related to the activities of the security-based swap execution facility; and (2) submit to onsite inspection and examination by representatives of the Commission with respect to the activities of the SB SEF, as required by proposed Rule 801(e). Finally, the applicant would be required to certify that, if it is a non-resident person, it can, as a matter of law, (1) provide the Commission with prompt access to its books and records and (2) submit to an onsite inspection and examination by representatives of the Commission, as required by proposed Rule 801(f).

Proposed Exhibit A to Form SB SEF would require the applicant to provide a copy of the governing documents of the applicant, including but not limited to a corporate charter, articles of incorporation or association, limited liability company agreement, or partnership agreement, with all subsequent amendments, and by-laws or corresponding rules or instruments, whatever the name, of the applicant. This information is intended to be used to assess the applicant's compliance with Core Principle 1 (Compliance with Core Principles), Core Principle 2 (Compliance with Rules), and Core Principle 11 (Conflicts of Interest). The information provided in this proposed exhibit is designed to allow the Commission to confirm that the applicant has the appropriate authority to operate the trading system and to regulate its participants, and that the ownership structure is consistent with the Exchange Act and the rules and regulations thereunder relating to the governance of SB SEFs.

Proposed Exhibit B to Form SB SEF would require the applicant to provide a copy of all written rulings, settled practices having the effect of rules, stated policies and interpretations of the Board or other committee of the applicant in respect of any provisions of the governing documents, rules or trading practices of the applicant which are not included in Exhibit A. This information required in proposed Exhibit B would be critical to the Commission's ability to assess the applicant's compliance with all of the Core Principles that require SB SEFs to establish and enforce rules relating to a variety of matters (*e.g.,* Core Principle 2 (Compliance with Rules); Core Principle 4 (Monitoring of Trade and Trade Processing); Core Principle 5 (Ability to Obtain Information); Core Principle 6 (Financial Integrity of Transactions); Core Principle 7 (Emergency Authority); Core Principle 10 (Antitrust Considerations); and Core Principle 11 (Conflicts of Interest)). Consequently, the Commission believes that such information is necessary for the Commission to confirm that the applicant's rules meet the requirements of those Core Principles and of the Exchange Act and the rules and

regulations thereunder, including proposed Regulation SB SEF.

Proposed Exhibit C to Form SB SEF would require the applicant to provide a list of the officers and directors of the SB SEF, or persons performing similar functions, who presently hold or have held their offices or positions during the previous year, and a list of all standing committees and their members, indicating the following for each: their name and title; date of commencement and termination of term of office or position; the type of business in which each is primarily engaged (*e.g.,* SB swap dealer, major SB swap participant, inter-dealer broker, end-user *etc.*); and, if such person is a director, whether such director qualifies as an "independent director" pursuant to proposed Rule 800 under Regulation SB SEF and whether such director is a member of any standing committees or committees that have the authority to act on behalf of the Board or the nominating committee. The Commission believes that mandating SB SEFs to disclose this information should better inform the Commission about SB SEF officers, the persons responsible for the day-to-day operation of the SB SEF, and SB SEF directors, the persons that comprise the Board. In addition, the Commission believes that the information required in Exhibit C is necessary for the Commission to determine the applicant's compliance with the governance requirements of Core Principle 11 (Conflicts of Interest) and the proposed rules under Regulation SB SEF relating thereto, and would aid the Commission in ascertaining any affiliations and relationships that would preclude directors from being considered independent.

Proposed Exhibit D to Form SB SEF would require an applicant to provide a chart or charts illustrating fully the internal organizational structure of the SB SEF. The charts would need to indicate the internal divisions or departments, the responsibilities of each such division or department, and the reporting structure of each division or department, including its oversight by committees or their equivalent. The charts should be sufficiently detailed to permit the Commission and the public to gain a complete understanding of the manner in which the SB SEF is structured and should be able to provide the Commission with an overview of the entity's organizational structure. The Commission preliminarily believes that disclosure of these organizational charts would be an important means by which to provide the Commission with a better understanding of the governance structure of the SB SEF and would enable the Commission to determine the applicant's compliance with Core Principle 11 (Conflicts of Interest) and the proposed rules under Regulation SB SEF relating thereto. In addition, the Commission preliminary believes that these organizational charts would inform the Commission's view on the ability of the SB SEF to carry out its regulatory and oversight responsibilities with respect to its markets.

Proposed Exhibit E to Form SB SEF would require an applicant to provide certain ownership information. Specifically, Exhibit E would require a list of each person that has a direct or indirect ownership or voting interest in the SB SEF that equals or exceeds 5%, and a list of all related persons of such persons that have an ownership or voting interest in the SB SEF or that are SB SEF participants. For each of the persons and related persons listed in the Exhibit E, an applicant would also need to provide such person's name, title or legal status and whether such person is a SB SEF participant; the date such title, status or participation in a SB SEF was acquired or commenced; the percentage ownership interest held; the type of ownership held, including whether such ownership interest qualifies as "beneficial ownership" under proposed Rule 800 or is entitled to vote; the percentage of voting interest held; and the type of voting interest held. The purpose of this information is to provide the Commission, participants of the SB SEF, and investors with detailed information about which persons or groups of persons potentially could control or influence the SB SEF. In addition, the information proposed to be required by Exhibit E relating to ownership of a SB SEF would provide the Commission, as well as participants in the SB SEF, with up-to-date information regarding a change or potential change in control of a SB SEF. The Commission expects that the disclosure of information concerning persons that hold ownership or voting interests of more than 5% of a SB SEF should help the Commission more effectively oversee and regulate SB SEFs, especially if the SB SEF is owned or controlled by persons who are not regulated by the Commission.

Proposed Exhibit F to Form SB SEF would require an applicant to provide, for the latest two fiscal years of the applicant, audited financial statements, which would be prepared in accordance with the same requirements for the preparation of financial statements submitted pursuant to the proposed rules under Regulation SB SEF relating to Core Principle 14.[343] The Commission preliminarily believes that this information would enable the Commission to assess the applicant's compliance with Core Principle 12 (Financial Resources) and the proposed rules under Regulation SB SEF relating thereto. In addition, the Commission believes that disclosure of audited financial statements would permit the Commission to better understand the financial resources and decisions of SB SEFs. The Commission preliminarily believes that these statements should be submitted by SB SEFs pursuant to Form SB SEF in addition to the rules relating to Core Principle 14, because documents submitted pursuant to Form SB SEF will be disclosed to the public. This would allow the public to be informed about the financial position of these SB SEFs and should facilitate investor confidence in the markets. In addition, because Exhibit F and the rules relating to Core Principle 14 have the same requirements with respect to the preparation and presentation of such financial statements, this should not create an additional burden on SB SEFs.

Proposed Exhibit G to Form SB SEF would require an applicant to provide an executed or executable copy of any agreements or contracts entered into or to be entered into by the applicant, or a subsidiary or an affiliate of the applicant, including partnership or limited liability company, third-party regulatory service, or other agreements relating to the operation of an electronic trading system to be used to effect transactions on the SB SEF ("System") that enable or empower the applicant to comply with Section 3D of the Exchange Act. The Commission believes that the provision of these material agreements would be useful for the Commission and the public. They would enable the Commission to understand how and through what parties the System is being operated and to have a better understanding of the arrangements that the SB SEF has entered into to meet its obligations under the Exchange Act. The information required in this exhibit would allow the Commission generally to ascertain the applicant's compliance with all Core Principles.

Proposed Exhibit H to Form SB SEF would require an applicant to provide unconsolidated financial statements (in English) for the latest two fiscal years for every subsidiary in which the applicant has, directly or indirectly, a 25% interest and every entity that has, directly or indirectly, a 25% interest in

[343] *See supra* Section XX.C for a discussion of the financial statement requirements pursuant to Core Principle 14. *See also* proposed Rule 823.

the applicant, which would be prepared in accordance with the same requirements for the preparation of financial statements submitted pursuant to the proposed rules under Regulation SB SEF relating to Core Principle 14.[344] Such financial statements would be required to contain such footnotes and other disclosures as are necessary to avoid rendering the financial statements misleading, and be provided in eXtensible Business Reporting Language consistent with Rules 405(a)(1), (a)(3), (b), (c), (d), and (e) of Regulation S–T.[345] In addition to the foregoing, for all other affiliates of the applicant not listed, such information would be required to be made available to the Commission upon request.[346] The Commission preliminarily believes that the information required in this exhibit would allow the Commission to assess the SB SEF's compliance with Core Principle 12 (Financial Resources) and the proposed rules under Regulation SB SEF relating thereto. In addition, the Commission believes that the required financial statement would enable the Commission to better understand the financial resources and decisions of SB SEFs and their affiliates. Finally, while evaluating an applicant's registration application on Form SB SEF, the Commission may determine that additional affiliates of the applicant that do not meet the 25% threshold may be material to the applicant's operation as a SB SEF. Therefore, the Commission preliminarily believes that it is appropriate to require an applicant to provide financial information regarding other affiliates upon request of the Commission.

Proposed Exhibit I to Form SB SEF would require an applicant to describe the manner of operation of the System. This description would be required to include: (1) A detailed description of the manner in which the System satisfies the definition of "security-based swap execution facility" in Section 3(a)(77) of the Exchange Act and any Commission rules, interpretations or guidelines regarding such definition, including a description of how the System displays all orders, quotes, requests for quote, responses, and trades in an electronic or other form, and the timelines in which the system does so; how trading interest interacts on the System; the ability of market participants to see and transact with orders, quotes, requests for quotes, and responses; and an explanation of the trade-matching algorithm if it is based on order priority factors other than price and time; (2) the means of access to the System, including any limitations on access; (3) procedures governing entry and display of trading interest in the System; (4) procedures governing the execution, reporting, clearance and settlement of transactions in connection with the System; (5) proposed fees; (6) procedures for ensuring compliance with System usage guidelines and rules; (7) the hours of operation of the System, and the date on which the applicant intends to commence operation of the System; (8) a copy of the users' manual or equivalent document; (9) if applicant proposes to hold funds or securities on a regular basis, a description of the controls that would be implemented to ensure safety of those funds or securities; and (10) the name of any entity, other than the SB SEF, that will be involved in operation of the System, including the execution, trading, clearing and settling of transactions on behalf of the SB SEF, and a description of the role and responsibilities of each entity.

The Commission believes that Exhibit I would allow the Commission to determine if the applicant meets the definition of SB SEF under the Exchange Act and rules and regulations hereunder, and in accordance with the guidance set forth in Section III above. In addition, Exhibit I would address the applicant's compliance with several Core Principles, including Core Principle 1 (Compliance with Rules), Core Principle 4 (Monitoring of Trade & Trade Processing), Core Principle 6 (Financial Integrity of Transactions), Core Principle 8 (Timely Publication of Trading Information), Core Principle 9 (Recordkeeping and Reporting), and Core Principle 13 (System Safeguards), and the proposed rules under Regulation SB SEF relating to such Core Principles.

Proposed Exhibit J to Form SB SEF would require an applicant to provide a complete set of all forms pertaining to: (1) Applications for participation or subscription to or use of the SB SEF; (2) applications for approval as a person associated with a SB SEF participant, or user of the SB SEF; and (3) any other similar materials. The applicant would have to provide a table of contents listing the forms included. The Commission believes that the information required in proposed Exhibit J would provide the Commission with important information on the ability of persons to directly access the SB SEF. Such information would enable the Commission to assess the applicant's compliance with Core Principle 2 (Compliance with Rules), Core Principle 5 (Ability to Obtain Information), and Core Principle 6 (Financial Integrity of Transactions) and the proposed rules under Regulation SB SEF related to such Core Principles.

Proposed Exhibit K to Form SB SEF would require an applicant to provide a complete set of all forms of financial statements, reports, or questionnaires required of SB SEF participants, subscribers or any other users relating to financial responsibility or minimum capital requirements for such participants or any other users. The applicant also would have to provide a table of contents listing the forms included. The Commission preliminarily believes that the information collected in this proposed exhibit would provide the Commission with the financial information that SB SEF's require of their participants and users and enable the Commission to assess the applicant's compliance with Core Principle 6 (Financial Integrity of Transactions) and the proposed rules under Regulation SB SEF related thereto.

Proposed Exhibit L to Form SB SEF would require an applicant to describe the applicant's criteria for participation in or use of the SB SEF. The applicant would be required to describe conditions under which SB SEF participants or persons associated with SB SEF participants may be subject to suspension or termination with regard to access to the SB SEF, and any procedures that would be involved in the suspension or termination of a SB SEF participant or person associated with a SB SEF participant. Proposed Exhibit L would require a SB SEF to provide a list of all grants of access (including, for all participants, the reasons for granting such access) and all denials or limitations of access (including, for each applicant or participant, the reasons for denying or limiting access). In addition, proposed Exhibit L would require a SB SEF to provide a list of all disciplinary actions taken by the SB SEF. The Commission preliminarily believes that proposed Exhibit L would provide the Commission with information regarding access to, limitations of access by, and

[344] *See supra* Section XX.C for a discussion of the financial statement requirements pursuant to Core Principle 14. *See also* proposed Rule 823.

[345] These requirements are the same as the requirements for the preparation of financial statements for affiliated entities that would be submitted pursuant to the proposed rules under Regulation SB SEF relating to Core Principle 14. *See supra* Section XX.C for a discussion of the financial statement requirements pursuant to Core Principle 14.

[346] This requirement to provide the information for all other affiliates of the applicant upon request is not contained in the rules under Regulation SB SEF relating to Core Principle 14, as the financial report submitted by the SB SEF pursuant to such rules is an annual report, rather than a registration application.

denials of access by a SB SEF, and disciplinary actions taken by a SB SEF against participants, and would allow the Commission to ascertain the applicant's compliance with Core Principle 2 (Compliance with Rules) and Core Principle 4 (Monitoring of Trading and Trade Processing) and the proposed rules under Regulation SB SEF relating to such Core Principles.

Proposed Exhibit M to Form SB SEF would require an applicant to provide an alphabetical list of all SB SEF participants or other users of the SB SEF, including the following information: name; date of acceptance as a participant or other user; principal business address and telephone number; if participant or other user is an individual, the name of the entity with which such individual is associated and the relationship of such individual to the entity (*e.g.,* partner, officer, director, employee, *etc.*); a description of the type of activities primarily engaged[347] in by the participant or other user (*e.g.,* SB swap dealer, major SB swap participant, inter-dealer broker, non-broker dealer, non-security-based swap dealer, commercial end-user, inactive or other functions); and the class of participation or other access. The Commission preliminarily believes that this exhibit would provide the Commission with information relating to who has access to trading on the SB SEF and would enable the Commission to determine whether a SB SEF is in compliance with Core Principle 2 (Compliance with Rules), Core Principle 6 (Financial Integrity of Transactions) and Core Principle 11 (Conflicts of Interest) and the proposed rules under Regulation SB SEF related to such Core Principles.

Proposed Exhibit N to Form SB SEF requires an applicant to provide a description of the criteria used to determine the SB swaps that may be traded on the SB SEF. The Commission preliminarily believes that this requirement would provide the Commission with information regarding the process by which a SB SEF determines what SB swaps would be traded on the SB SEF and the factors the SB SEF would consider in making such determination. Proposed Exhibit O to Form SB SEF requires an applicant to provide a schedule of the SB swaps to be traded on the SB SEF, including a description of each SB swap. The Commission believes that proposed Exhibits N and O would enable the Commission to determine whether a SB SEF is complying with Core Principle 2 (Compliance with Rules), Core Principle 6 (Financial Integrity of Transactions) and Core Principle 3 (Security-based Swaps not Readily Susceptible to Manipulation) and the proposed rules under Regulation SB SEF relating to such Core Principles.

Proposed Exhibit P to Form SB SEF would require an applicant that is controlled by any other person to provide an opinion of counsel that any person that controls the SB SEF has consented to and can, as a matter of law, (1) provide the Commission with prompt access to its books and records, to the extent such books and records are related to the activities of the SB SEF; and (2) submit to onsite inspection and examination by representatives of the Commission with respect to the activities of the SB SEF. Proposed Exhibit P to Form SB SEF also would require an applicant that is a non-resident person to provide an opinion of counsel that the applicant can, as a matter of law, (1) provide the Commission with prompt access to the books and records of such applicant and (2) submit to onsite inspection and examination by representatives of the Commission. As discussed in Section XXI above, these requirements would allow the Commission to better evaluate an applicant's ability to comply with the books and records and inspection requirements set forth in proposed Rules 801(e) and (f).

A national securities exchange that seeks to operate a SB SEF would be required to separately register such SB SEF with the Commission as a SB SEF pursuant to proposed Rule 801 and proposed Form SB SEF, and would be required to comply with Section 3D of the Exchange Act, the rules and regulations thereunder, and any other provisions of the Exchange Act and rules thereunder applicable to SB SEFs with respect to the operations of such SB SEF.

National securities exchanges could, under the rules the Commission is proposing today, form subsidiaries or affiliates that operate SB SEFs. If a national securities exchange chose to form such a subsidiary or affiliate, the exchange itself could remain registered as a national securities exchange, while the subsidiary or affiliate registers and operates as a SB SEF. Section 3D(c) of the Exchange Act requires a national securities exchange to identify whether electronic trading of SB swaps is taking place on or through the national securities exchange or a SB SEF to the extent that the exchange also operates a SB SEF and uses the same electronic trade execution system for listing and executing trades of SB swaps. The Commission notes that any subsidiary or affiliate of a registered exchange could not integrate, or otherwise link the SB SEF with the exchange, including using the premises or property of such exchange for effecting or reporting a transaction, without being considered a "facility of the exchange."[348] In the event that a national securities exchange begins trading SB swaps either on the exchange or on a facility of the exchange, it would be required to file rule filings under Rule 19b–4 under the Exchange Act in connection with the trading of SB swaps on the exchange or its facility, and such facility would have to comply with the provisions of the Exchange Act and the rules and regulations thereunder applicable to national securities exchanges.

The Commission generally requests comments on all aspects of the proposed Form SB SEF. Is the format of the proposed Form SB SEF appropriate and sufficiently clear? If not, why not and how could it be improved? Are the instructions to the proposed Form SB SEF appropriate and sufficiently clear? If not, why not and how could they be improved? Are the defined terms included on proposed Form SB SEF appropriate and sufficiently clear? If not, why not and how could they be improved?

Are the disclosure items contained on the Execution Page of the proposed Form SB SEF appropriate? Are there other useful disclosure items that should be added? If so, please describe such items and why they should be added. Or, are there proposed items on the Execution Page that should be deleted? If so, please describe why such items are not necessary. Are the certifications contained on the Execution Page of the proposed Form SB SEF appropriate? Are there other useful certifications that the Commission should require the applicant to make? If so, please describe such items and why they should be added. Or, are there proposed certifications that should be deleted? If so, please describe why such certifications are not necessary.

Are the proposed exhibits to the Form SB SEF appropriate? Would the

[347] A person would be "primarily engaged" in an activity or function for purposes of this item when that activity or function is the one in which that person is engaged for the majority of their time. When more than one type of person at an entity engages in any of the types of activities or functions enumerated in this item, the applicant would be required to identify each type and state the number of participants or other users in each.

[348] *See* Section 3(a)(2) of the Exchange Act, 15 U.S.C. 78c(a)(2) (defining the term "facility of the exchange"). The Commission gave a similar analysis regarding facilities of exchanges with regard to ATSs in the ATS Adopting Release, *supra* note 94, at note 437.

information requested adequately allow the Commission to determine whether to grant or deny the registration of a SB SEF pursuant to proposed Rule 801(b)? Are there other useful disclosure items that should be added to the exhibits or added as exhibits? If so, please describe such items and why they should be added. Are there any registration requirements proposed by the CFTC for SEFs that the Commission should adopt for SB SEFs? [349] For example, should the Commission require a SB SEF to provide a description of material pending legal proceedings? [350] Should the Commission require a SB SEF to provide a description of the personnel qualifications for each category of professional employees employed by the applicant? [351] Should the Commission require a SB SEF to provide an analysis of the staffing requirements necessary to carry out operations of the applicant and the name and qualifications of each key staff person? [352] Is the information requested on Form SB SEF and the exhibits thereto overly burdensome for SB SEFs? If so, how could any such burdens be reduced? Are there proposed exhibits or items of information in proposed exhibits that should be deleted from proposed Form SB SEF? If so, please describe why such proposed exhibits would not be necessary. Should certain proposed exhibits be required to be made available to the Commission only upon request? If so, which proposed exhibits and why? For example, should an applicant be required to provide the information regarding SB SEF participants required by proposed Exhibit M upon request by the Commission following the filing of the applicant's Form SB SEF, rather than as an exhibit to the applicant's initial filing of proposed Form SB SEF? Commenters are requested to consider the totality of the information required by proposed Form SB SEF in framing their responses.

The Commission also requests that commenters address whether there are confidentiality issues with any information required by the proposed exhibits to proposed Form SB SEF? If so, what information presents issues and what are the issues? Further, the Commission notes that proposed Form SB SEF would be filed electronically and thus is expected to be made available publicly on the Commission's Web site. The Commission seeks comment on whether the information to be filed on proposed Form SB SEF would be useful to the public.

XXIII. Rule Filing Processes for Changes to a SB SEF's Rules

A. Introduction

The Commission is proposing to adopt rules requiring registered SB SEFs to comply with certain rule filing processes for any new rules or rule amendments. Specifically, the Commission is proposing new Rules 805 and 806, which set forth, respectively, a process for the voluntary submission of rules for Commission review and approval, and a self-certification rule filing process.[353] The processes proposed under these rules are substantially similar to the two rule filing processes that the CFTC has in its existing rules,[354] as modified by the new authority the CFTC has received under Section 745 of the Dodd-Frank Act.[355] It is important for the Commission to receive notice of proposed rule changes to understand how each SB SEF operates and is governed to help the Commission with its oversight of SB SEFs. The Commission intends to coordinate efforts with the CFTC, as appropriate, to have the processes offered in proposed Rules 805 and 806 resemble the rule filings processes that the CFTC ultimately adopts for SEFs, in large part to streamline and simplify compliance for joint SEF/SB SEF entities.

B. Voluntary Submission of Rules for Commission Review and Approval

Proposed Rule 805 gives a registered SB SEF the option of voluntarily submitting a proposed new rule or rule amendment for approval by the Commission prior to its implementation. Paragraph (a) of proposed Rule 805 would require such filings to: (1) Be filed electronically with the Commission in a format specified by the Commission; (2) set forth the text of the proposed rule or rule amendment (in the case of a rule amendment, deletions and additions must be indicated); (3) indicate the proposed effective date of the proposed rule, any action taken or anticipated to be taken to adopt the proposed rule by the SB SEF or by its governing board or by any committee thereof, and the cite for the rules of the SB SEF that authorize the adoption of the proposed rule change; (4) explain the operation, purpose, and effect of the proposed rule, including, as applicable, a description of the anticipated benefits to market participants or others, any potential anticompetitive effects on market participants or others, and how the rule fits into the SB SEF's framework of regulation; (5) certify that the SB SEF posted a notice of pending rule filing and a copy of the submission, concurrent with the filing of a submission on its Web site; (6) include the documentation relied on to establish the basis for compliance with the applicable provisions of the Exchange Act and the Commission's regulations thereunder, including the Core Principles; (7) provide additional information which may be beneficial to the Commission in analyzing the new rule or rule amendment; (8) describe briefly any substantive opposing views expressed to the SB SEF by the Board or committee members, participants of the SB SEF, or market participants with respect to the new rule or rule amendment that were not incorporated into the new rule or rule amendment; (9) identify any Commission regulation that the Commission may need to amend, or sections of the Exchange Act or the Commission's regulations that the Commission may need to interpret, in order to approve the new rule or rule amendment; (10) in the case of proposed amendments to the terms and conditions of a SB swap product, include a written statement verifying that the registered SB SEF has undertaken a due diligence review of the legal conditions, including conditions relating to contractual and intellectual property rights, that may materially affect the trading of the product; and (11) request confidential treatment, if appropriate.[356]

Proposed Rule 805(a) sets forth the information a SB SEF would be required to provide the Commission when seeking Commission approval of a proposed change to a SB SEF rule, or a proposed change to the terms and conditions of a SB swap that has already commenced trading. Most of the proposed items of information to be included are substantially similar to the items of information a national securities exchange is required to provide on Form 19b–4 [357] when

[349] *See* Notice of proposed SEF rulemaking by the CFTC Release, *supra* note 17.

[350] *See* proposed Exhibit H to proposed Form SEF; *see also* Notice of proposed SEF rulemaking by the CFTC, *supra* note 17.

[351] *See* proposed Exhibit E to proposed Form SEF; *see also* Notice of proposed SEF rulemaking by the CFTC, *supra* note 17.

[352] *See* proposed Exhibit F to proposed Form SEF; *see also* Notice of proposed SEF rulemaking by the CFTC, *supra* note 17.

[353] Proposed Rule 806(d) also provides a limited exception to the certification requirement for certain kinds of filings. *See* proposed Rule 806(d). *See also* discussion *infra* notes 382 to 384 and accompanying text.

[354] 17 CFR 40.5 and 17 CFR 40.6.

[355] *See* Public Law 111–203 § 745 (amending Section 5c of the CEA, 7 U.S.C. 7a–2).

[356] *See* proposed Rule 805(a).

[357] *See* 17 CFR 240.19b–4.

seeking approval of a proposed rule change in accordance with Section 19(b) of the Exchange Act.[358] Specifically, the requirements in proposed Rule 805(a)(1) through (4) regarding electronic submission, submission of proposed rule text highlighting additions and deletions, inclusion of background information on how and why a proposed change is authorized, and explanation of the operation, purpose, and effect of the proposed rule change are similar to the requirements applicable to national securities exchanges seeking to implement a proposed rule change. Further, the requirements in proposed Rule 805(a)(7) through (9) to include additional information beneficial to the Commission in analyzing the new rule or rule amendment, a description of substantive opposing views expressed to the SB SEF regarding the proposal, and to identify any Commission regulation that the Commission may need to amend or interpret in order to approve the new rule or rule amendment also are similar to the requirements of Form 19b–4 applicable to national securities exchanges. These requirements are designed to ensure that a SB SEF seeking to implement a new or proposed rule change provides all relevant information and context regarding the proposal that would allow the Commission to evaluate the proposal for consistency with the Exchange Act and rules and requirements thereunder.

In addition, similar to the requirements for national securities exchanges, the proposal in Rule 805(a)(5) would require a SB SEF to certify that it has posted a notice of pending rule filing and a copy of the submission, concurrent with the filing of a submission on its Web site. This proposal is intended to ensure that market participants would receive prompt notice of new requests for approval filed with the Commission.[359]

Proposed Rule 805(a)(6) also would require a SB SEF to include the documentation relied on to establish the basis for compliance with the applicable provisions of the Exchange Act and the Commission's regulations thereunder, including the Core Principles. In the case of proposed changes to the terms and conditions of a SB swap, this provision would require, without limitation, inclusion of documentation relied on to establish the basis for compliance with Section 3D(d)(3) of the Exchange Act and proposed Rule 812 thereunder, which would require a SB SEF's swap review committee to have determined, after taking into account all of the terms and conditions of the SB swap and the markets for the SB swap and any underlying securities, that a SB swap proposed to be traded is not readily susceptible to manipulation.[360]

Also with regard to proposed changes to the terms and conditions of a SB swap, proposed Rule 805(a) would require a SB SEF to provide a written statement verifying that it has undertaken a due diligence review of the legal conditions, including conditions relating to contractual and intellectual property rights, that may materially affect the trading the product. This proposed requirement is designed to prevent a SB SEF from seeking to trade a proprietary product of another SB SEF or other entity. The Commission preliminarily believes that the information to be included pursuant to proposed Rule 805(a) in a request for approval of a new or proposed rule change or change to the terms and conditions of a SB swap is necessary to assist the Commission in making a reasoned determination as to whether such proposed change is consistent with the Exchange Act.

Proposed Rule 805(b) would require the Commission to approve a new rule or rule amendment unless the rule or rule amendment is inconsistent with the Exchange Act or the Commission's regulations promulgated thereunder.[361] The Commission has coordinated with the CFTC and the proposed standard for approval is the same as that standard for approval under the CFTC's proposed rule approval process, which is intended to provide consistency to market participants who may operate a SB SEF and a SEF.

Proposed Rule 805(c) would give the Commission a 45-day review period, starting from the date that the filing is received by the Commission, to consider whether the proposed rule or rule amendment is consistent with the Exchange Act and the regulations thereunder.[362] Unless the Commission notifies the SB SEF otherwise, the proposed rule change would be deemed approved by the Commission at the end of the 45-day review period (or at the end of any extension period, as applicable), provided that: (1) The submission of the rule change complies with the requirements of paragraph (a) of proposed Rule 805, and (2) the SB SEF has not amended the filing during the review period, except as requested by the Commission during that period.[363]

Under paragraph (d) of proposed Rule 805, the Commission would be able to extend the review period by an additional 45 days if the proposed rule raises novel or complex issues that require additional time for review or is of major economic significance, the submission is incomplete, or the requestor does not respond completely to Commission questions in a timely manner.[364] In this case, the Commission would be required to notify the submitting SB SEF within the initial 45-day review period and briefly describe the nature of the specific issues for which additional time for review is required. In addition, the Commission would be able to extend the review period to any period, beyond the additional 45 days initially requested, to which the SB SEF agrees in writing.[365]

Under paragraph (e) of proposed Rule 805, the Commission would have the authority to issue a notice of non-approval if it finds that the new rule or rule amendment is or appears to be inconsistent with the Exchange Act or the regulations thereunder.[366] At any time during its review under proposed Rule 805, the Commission would be able to notify the SB SEF that it will not approve the new rule or rule amendment because it believes that the new rule or rule amendment is inconsistent with the Exchange Act or Commission rules or regulations thereunder. The Commission would provide, in its notice, the nature of the issues raised and the specific provision of the Exchange Act or the Commission's rules or regulations with which the new rule or rule amendment is or appears to be inconsistent. Pursuant to proposed Rule 805(f), the receipt of a notice of non-approval would not prevent the SB SEF from subsequently submitting a revised version of the proposed rule or rule amendment for Commission review and approval, and the revised submission would be reviewed without prejudice.[367] However, the receipt of a notice of non-approval would be presumptive evidence that the SB SEF could not truthfully submit the same, or substantially the same, proposed rule or

[358] 15 U.S.C. 78s(b).

[359] Rule 19b–4(*l*) under the Exchange Act requires each national securities exchange to post proposed rule changes on its Web site within two business days of filing with the Commission. *See* 17 CFR 240.19b–4(*l*).

[360] *See* Proposed Rule 812.

[361] *See* proposed Rule 805(b).

[362] *See* proposed Rule 805(c).

[363] *Id.* Any amendment or supplementation not requested by the Commission would be treated as the submission of a new filing.

[364] *See* proposed Rule 805(d).

[365] *Id.*

[366] *See* proposed Rule 805(e).

[367] *See* proposed Rule 805(f)(1).

rule amendment for self-certification under proposed Rule 806.[368]

Proposed Rule 805(g) would allow the Commission to provide for expedited approval for rule changes, including rule changes to terms and conditions of a product that are consistent with the Exchange Act and the rules and regulations thereunder, at such time and under such conditions as the Commission may specify in a written notification.[369] However, proposed Rule 805(g) would also allow the Commission to grant expedited approval to a proposed rule or rule amendment, at any time, and also to alter or revoke the applicability of such a notice to any particular rule or rule amendment.

The Commission is proposing the time periods in paragraphs 805(c) through (g) to align its procedure for reviewing proposed rules and rule amendments with the CFTC's procedure.[370] The Commission believes that a parallel procedure would be beneficial for SB SEFs and SEFs that are dually registered. Furthermore, the Commission believes that the proposed prior approval process would allow the SB SEF the opportunity to achieve greater certainty about the Commission's views on whether a new rule or rule amendment is consistent with the Exchange Act and the rules and regulations thereunder prior to taking steps to implement the rule or amendment.

C. Self-Certification of Rules

Proposed Rule 806 would allow a SB SEF, as an alternative to complying with proposed Rule 805, to implement a new rule or rule amendment pursuant to self-certification.[371] This process would provide the Commission ten business days to review a self-certification filing and to stay the certification within such review period, if warranted.

Specifically, under proposed Rule 806(a), a registered SB SEFs would be required to submit the self-certification electronically at least ten business days prior to the implementation date of the new rule or rule amendment.[372] The proposed rule would require that the SB SEF publish on its Web site a notice of pending certification with the Commission and copy of the submission concurrent with the filing of a submission with the Commission.[373]

Similar to proposed Rule 805, proposed Rule 806 would require the submission to include certain specific items: (1) The text of the rule (in the case of a rule amendment, deletions and additions must be indicated); (2) the date of intended implementation; (3) a certification by the SB SEF that the rule complies with the Exchange Act and the Commission's regulations thereunder; (4) the documentation relied on to establish the basis for compliance with the applicable provisions of the Exchange Act and the Commission's regulations thereunder, including the Core Principles;[374] (5) a brief explanation of any substantive opposing views expressed to the registered SB SEF by the Board or committee members, participants, or market participants that were not incorporated into the rule, or a statement that no such opposing views were expressed; (6) a request for confidential treatment, if appropriate; and (7) in the case of proposed amendments to the terms and conditions of a SB swap, a written statement verifying that the registered SB SEF has undertaken a due diligence review of the legal conditions, including conditions relating to contractual and intellectual property rights, that may materially affect the trading the product.[375] The proposed Rule would also require the SB SEF to provide, if requested by Commission staff, additional evidence, information or data that may be beneficial to the Commission in conducting a due diligence assessment of the filing and the SB SEF's compliance with any of the requirements of the Exchange Act or the Commission's rules or regulations thereunder.[376] The proposed items of information are similar to those required by proposed Rule 805(a) as well as those in CFTC Rule 40.6.[377] The Commission preliminarily believes that inclusion of the items of information set forth in proposed Rule 806(a) would assist the Commission in considering whether a SB SEF's implementation of a new rule, rule amendment, or modification to the terms and conditions of a SB swap pursuant to self-certification is appropriate and consistent with the Exchange Act and the rules and requirements thereunder.

Under paragraph (b) of proposed Rule 806, the Commission would have 10 business days to review the submission and the self-certification would become effective at the end of the 10 business-day period, unless the Commission notifies the registered entity, during such 10 business-day period, that it intends to issue a stay of the certification.[378] Proposed Rule 806(c)(1) would provide that the Commission would be able to stay the certification of a new rule or rule amendment by issuing a notification to the SB SEF informing it that the Commission is staying the certification and stating the grounds for doing so.[379] The proposed rule also would provide that the certification of a rule could be stayed by the Commission on the grounds that the new rule or rule amendment presents novel or complex issues, is accompanied by an inadequate explanation, or is potentially inconsistent with the Exchange Act or the Commission's regulations thereunder. Once the Commission issues a notification of stay to the registered entity, the Commission would have 90 days to conduct a review. A stay of a rule certification may be appropriate, for example, where a registered entity certifies a rule that raises unique issues not previously reviewed by Commission staff. In addition, the Commission believes that new rules or rule amendments may raise a number of complex issues if they appear to have a material impact on other securities and financial markets. Thus, such rules are more likely to be

[368] *See* proposed Rule 805(f)(2). *See infra* Section XXIII for a discussion of the certification process.

[369] *See* proposed Rule 805(g).

[370] *See* 17 CFR 40.5 and 40.6. *See also* Public Law 111–203, § 745 (amending Section 5c of the Commodity Exchange Act, 7 U.S.C. 7a–2). *See also* 75 FR 67282 (November 2, 2010) (CFTC proposal to amend 17 CFR 40.5 and 40.6).

[371] *See* proposed Rule 806.

[372] *See* proposed Rule 806(a)(1) and proposed Rule 806(a)(3). Proposed Rule 806(a)(3) would provide an exception to the 10 day requirement for new rules or rule amendments that the SB SEF seeks to implement in the exercise of its emergency authority pursuant to Rule 816, requiring instead that the SB SEF file such emergency rule or rule amendment with the Commission prior to the implementation of such rule or rule amendment, or, if not practicable, within twenty-four hours after implementation of such emergency rule or rule amendment.

[373] *See* proposed Rule 806(a)(2). The proposed Rule would require the SB SEF to provide such information in its submission to the Commission, but would permit the SB SEF to redact information that it seeks to keep confidential from the documents that it publishes on its Web site. If, however, a determination is made pursuant to the Freedom of Information Act that such information may not be kept confidential, the proposed rule would require the SB SEF to republish its filing on its Web site including such information.

[374] In the case of proposed changes to the terms and conditions of a SB swap, this provision would require, without limitation, inclusion of documentation relied on to establish the basis for compliance with Section 3D(d)(3) of the Exchange Act and proposed Rule 812 thereunder, which would require a SB SEF's swap review committee to have determined, after taking into account all of the terms and conditions of the SB swap and the markets for the SB swap and any underlying securities, that a SB swap proposed to be traded is not readily susceptible to manipulation. *See* proposed Rule 812.

[375] *See* proposed Rule 806(a)(5).

[376] *See* proposed Rule 806(a)(6).

[377] *See* proposed Rule 805(a) and 17 CFR 40.6. *See also* Public Law 111–203, § 745 (amending Section 5c of the Commodity Exchange Act, 7 U.S.C. 7a–2).

[378] *See* proposed Rule 806(b).

[379] *See* proposed Rule 806(c)(1).

subject to an extended review period to allow the Commission to adequately identify and address complex regulatory issues.

Proposed Rule 806(c)(2) would require the Commission to provide a 30-day public comment period within the 90-day period that the stay is in effect and to publish a notice of the 30-day comment period on the Commission's Web site.[380] Unless the Commission notifies the SB SEF that it objects to the certification within the 90-day period on the grounds that the proposed rule is inconsistent with the Exchange Act or the rules or regulations thereunder, the rule would become effective, pursuant to certification, upon the expiration of the 90-day review period.[381] If the Commission decides to lift the stay prior to the expiration of the 90-day review period, the Commission would notify the SB SEF of its action and the rule would become certified at such time.

Finally, proposed Rule 806(d) would permit SB SEFs to implement certain new rules or rule amendments on the following business day without certification to the Commission.[382] Pursuant to proposed Rule 806(d)(1), the rules permitted to be implemented pursuant to this summary process would be limited to rules regarding corrections of typographical errors, renumbering, periodic routine updates to identifying information about approved entities and other such non-substantive revisions of a product's terms and conditions that have no effect on the economic characteristics of the product.[383] Proposed Rule 806(d)(2) would require SB SEFs to provide to the Commission electronically, in a format to be specified by the Commission, at least weekly, a summary notice of all rule amendments made effective thereunder.[384] Such notice would not be required for weeks during which no such actions have been taken. Proposed Rule 806(e) would allow a SB SEF to implement certain other new rules or rule amendments without certification or notice to the Commission, provided that the SB SEF maintains documentation regarding all changes to rules and posts all such rule changes on its Web site.[385] These rules and rule amendments would be those that govern: (1) The organization and administrative procedures of a SB SEF governing bodies such as a Board, officers, and committees, but not any of the following: Voting requirements; Board or committee composition requirements or procedures; decision making procedures; use or disclosure of material non-public information gained through the performance of official duties, or requirements relating to conflicts of interest; or (2) the routine, daily administration, direction and control of employees, requirements relating to gratuity and similar funds, but not any of the following: Guaranty; reserves; or similar funds; declaration of holidays; and changes to facilities housing the market.

The Commission notes that the certification process in proposed Rule 806 does not call for any final action by the Commission. In cases where a SB SEF seeks final agency action, a SB SEF could choose to file a proposed rule or rule amendment under proposed Rule 805.

The Commission intends to allow registered SB SEFs to submit filings under proposed Rules 805 and 806 electronically through a portal similar to the electronic rule filing system used for proposed rule changes by national securities exchanges and national securities associations.[386]

The Commission notes that the process under proposed Rules 805 and 806 closely parallel the CFTC's Rules 40.5 and 40.6.[387] The Commission preliminarily believes that allowing SB SEFs to file new rules and rule amendments in this manner would simplify the filing process and also provide the Commission with prompt access for review. The Commission intends to propose forms for these electronic filings as part of a separate rulemaking.

D. Request for Comment

The Commission generally requests comments on all aspects of the proposed rules relating to the proposed rule filing process. Are the Commission's proposed rules for the filing process for new rules and rule amendments appropriate and sufficiently clear? If not, why not and what would be better alternatives? Is it preferable to have a rule filing process for SB SEFs that closely aligns to the process for SEFs under the CFTC's rules as proposed? By doing this, would the proposed rules achieve the goal of streamlining and simplifying the effort to have rules implemented for entities that are both SB SEFs and SEFs? If not, what other alternatives should the Commission consider? What other burdens should the Commission take account of that joint SB SEF/SEF entities would face under the proposed rules? Is the voluntary prior approval process in proposed Rule 805 a useful option for SB SEFs? If not, what would be a better alternative?

Does the automatic effectiveness for a rule or rule amendment submitted under proposed Rule 806, once the review period has expired and in the absence of non-approval, provide sufficient legal clarity and certainty about the change? Or, would an approval order by the Commission be more instructive or helpful? Are the time periods for review, and extensions for review, in proposed Rule 805 appropriate? If so, what would be more appropriate? Should the submissions for prior approval be published by the Commission for public comment? Why or why not?

Is the provision of a notice of non-approval to the SB SEF, as described under proposed Rule 805(e), a sufficient means of informing the SB SEF of the basis for non-approval? Would more information or another form of notice be more appropriate? If so, please explain. Should such notice of non-approval be published on the Commission's Web site or otherwise be made publicly available? Would the proposed self-certification process in proposed Rule 806 be a useful alternative to the prior approval process for rule changes? Why or why not?

Are the proposed grounds for staying a certification under proposed Rule 806(c) appropriate? If not, why not? Are there other grounds that would also be appropriate for staying a certification? Under proposed Rule 806 (for self-certification), would the 10 business-day review period and, if a stay is put in place, the 90-day review period be appropriate timeframes for Commission review and consideration? If not, why not and what would be a better alternative? Please provide support for any alternative suggestions.

Should the 90-day review period, subsequent to a stay of a certification, in proposed Rule 806(c) include a 30-day public comment period? Why or why not? Is the means for determining whether a rule or rule amendment has been certified or objected to provided for in proposed Rule 806(c)(3) sufficiently clear? If not, how could such determination be made more clear? Should the Commission publish notice of either the effective certification or the notice of an objection for the public on its Web site or through other means?

[380] *See* proposed Rule 806(c)(2).

[381] *See* proposed Rule 806(c)(3).

[382] *See* proposed Rule 806(d).

[383] *See* proposed Rule 806(d)(2).

[384] *See* proposed Rule 806(d)(1).

[385] *See* proposed Rule 806(e).

[386] The process for submission of rule filings would be the subject of a separate rulemaking.

[387] *See* 17 CFR 40.5 and 40.6. *See also* Public Law 111–203, § 745 (amending Section 5c of the Commodity Exchange Act, 7 U.S.C. 7a–2). *See also* 75 FR 67282 (November 2, 2010) (CFTC proposal to amend 17 CFR 40.5 and 40.6.

Are the proposed processes for providing notice, without a certification, for certain kinds of rule changes in proposed Rule 806(d) appropriate? If not, why not? Are the proposed rule changes that would be eligible for notice without certification in proposed Rule 806(d) and (e) appropriate? If not, which ones should not be eligible for these processes? Are there other kinds of rule changes that should be eligible for these processes?

Would an electronic method for submitting all rule submissions under proposed Rules 805 and 806 be an appropriate and efficient way of making such submissions? If not, why not? Would an electronic system such as the existing system for submitting rule changes by national securities exchanges and associations, Electronic Form 19b–4 Filing System, or "EFFS,"[388] be a good model for the system for SB SEF submissions under these proposed rules? If not, what would be a better model for such an electronic system?

XXIV. Filing Processes for Trading Security-Based Swaps

A. Introduction

The Commission is proposing to adopt rules requiring SB SEFs to comply with certain filing processes prior to trading SB swaps. Specifically, the Commission is proposing new Rules 807 and 808 of Regulation SB SEF, which set forth filing processes for commencement or continued trading of SB swaps on a SB SEF. The processes proposed under these rules are substantially similar to the parallel processes that the CFTC has in its existing rules, 17 CFR 40.2 and 17 CFR 40.3, as modified by the new authority the CFTC has received under Section 745 of the Dodd-Frank Act.[389]

The proposed filing processes pursuant to which a SB SEF may trade a SB swap each require that a SB SEF describe the proposed product's "terms and conditions." The Commission is not proposing a definition of "terms and conditions," but requests comment on whether it should adopt a definition of "terms and conditions" and, if so, what specifically should such a definition include.[390] Specifically, should a Commission definition of "terms and conditions" refer to the rights and obligations of the counterparties to a SB swap? Should it include such items as: (1) Notional values; (2) relevant dates, tenor, and day count conventions; (3) index; (4) relevant prices, rates or coupons; (5) currency; (6) stub, premium, or initial cash flow components along with subsequent life cycle events; (7) payment and reset frequency; (8) business calendars; (9) accrual type; (10) spread or points; and (11) description of the underlying security or securities or reference asset(s)? Should it include other items that appear in the CFTC's definition? Are there any other items that should be included? Should the ISDA Master Agreement be referenced in a definition? If so, why and how?

B. Trading SB Swaps Pursuant to Certification

Proposed Rule 807 would require every SB SEF to comply with certain submission requirements prior to trading a SB swap product if such product has not been approved under proposed Rule 808. Pursuant to proposed Rule 807 every submission must be filed electronically in a form to be determined by the Commission and be received by the Commission by the open of business on the business day preceding the day the SB swap would commence trading. In addition, every submission would be required to include: (1) A copy of the SB swap product's terms and conditions; (2) the intended date on which the SB swap may begin trading; (3) a certification by the registered SB SEF that the SB swap to be traded complies with the Exchange Act and the rules and regulations thereunder; (4) the documentation relied on to establish the basis for compliance with the Exchange Act and the rules and regulations thereunder, including the Core Principles;[391] (5) a written statement verifying that the registered SB SEF has undertaken a due diligence review of the legal conditions, including legal conditions that relate to contractual and intellectual property rights, that may materially affect the trading of the SB swap; (6) a certification that the registered SB SEF posted on its Web site a notice of pending certification with the Commission and a copy of the submission, concurrent with the filing of a submission with the Commission; and (7) a request for confidential treatment, if appropriate.

Pursuant to proposed Rule 807(b), upon request of any representative of the Commission, a SB SEF would be required to provide any additional evidence, information or data demonstrating that the SB swap product meets, initially or on a continuing basis, all of the requirements of the Exchange Act and its rules.

Proposed Rule 807(c) would provide that the Commission would be able to stay the certification of a SB swap by issuing a notification to the SB SEF informing it that the Commission is staying the certification and stating the grounds for doing so.[392] The proposed rule also would provide that the certification could be stayed by the Commission on the grounds that the SB swap presents novel or complex issues, is accompanied by an inadequate explanation, or is potentially inconsistent with the Exchange Act or the Commission's regulations thereunder. Once the Commission issues a notification of stay to the registered entity, the Commission would have 90 days to conduct a review. A stay of a certification may be appropriate, for example, where a registered entity certifies a SB swap that raises unique issues not previously reviewed by Commission staff.

Proposed Rule 807(c) would require the Commission to provide a 30-day public comment period within the 90-day period that the stay is in effect and to publish a notice of the 30-day comment period on the Commission's Web site.[393] Unless the Commission notifies the SB SEF that it objects to the certification within the 90-day period on the grounds that the proposed SB swap is inconsistent with the Exchange Act or the rules or regulations thereunder, the SB swap would become effective, pursuant to certification, upon the expiration of the 90-day review period.[394] If the Commission decides to lift the stay prior to the expiration of the 90-day review period, the Commission would notify the SB SEF of its action

[388] *See* Securities Exchange Act Release No. 50486 (October 4, 2004), 69 FR 60287 (October 8, 2004) (File No. S7–18–04).

[389] *See* Public Law 111–203, § 745 (amending Section 5c of the Commodity Exchange Act, 7 U.S.C. 7a–2). *See also* 75 FR 67282 (November 2, 2010) (CFTC proposal to amend 17 CFR 40.2 and 40.3).

[390] The Commission notes that the CFTC, in 17 CFR 40.1, defines "terms and conditions" as referring to a description of the security underlying a swap, specification of cash settlement, and the rights and obligations of the counterparties to the swap. The CFTC's definition also notes that whenever possible, all proposed swap terms and conditions should conform to industry standards or those terms and conditions adopted by comparable contracts. Further, the CFTC's definition sets forth a list of items covered by the phrase "terms and conditions."

[391] As discussed in note 374 *supra,* this provision would require, without limitation, inclusion of documentation relied on to establish the basis for compliance with Section 3D(d)(3) of the Exchange Act and proposed Rule 812 thereunder, which would require a SB SEF's swap review committee to have determined, after taking into account all of the terms and conditions of the SB swap and the markets for the SB swap and any underlying securities, that a SB swap proposed to be traded is not readily susceptible to manipulation.

[392] *See* proposed Rule 807(c)(1).

[393] *See* proposed Rule 807(c)(2).

[394] *See* proposed Rule 807(c).

and the SB swap would become certified at such time.[395]

The Commission preliminarily believes that proposed Rule 807, which closely parallels CFTC proposed new Rule 40.2, provides a reasonable process pursuant to which a SB SEF may trade SB swaps through a certification process. Any dually registered SB SEF would be following very similar procedures for certification of swaps under CFTC proposed new Rule 40.2. The proposed rule would give the Commission notice of any new SB swaps for which a SB SEF would permit trading and would allow the Commission to stay a proposed SB swap's certification in certain circumstances. In addition, because the proposed rule closely parallels the CFTC's proposed rule, it would provide for greater harmonization of the regulatory process applied to SEFs and SB SEFs.

The Commission also preliminarily believes that it is appropriate to include in any submissions under proposed Rule 807 documentation demonstrating that the product is in compliance with the SB SEF Core Principles—in particular, core principles that apply specifically to products, such as Core Principle 3 concerning manipulation. The Commission preliminarily believes that it is appropriate to require a SB SEF to document the basis for a determination that a SB swap is not readily susceptible to manipulation and notes that the self-certification in proposed Rule 807 is drawn from analogous processes that the CFTC currently has in place with respect to new financial futures products proposed to be traded on a designated contract market.[396] The Commission further notes that CFTC regulations require that prior to trading a new product, a designated contract market must demonstrate that the terms and conditions of a proposed contract "will not be conducive to price manipulation or distortion."[397] The Commission also preliminarily believes that SB SEFs should be conducting due diligence before listing a new SB swap product. In evaluating any certification, information on such due diligence would be essential to the Commission.

The Commission preliminarily believes that SB SEFs would make use of the certification process in the same way that registered entities have been making use of the parallel process under the CFTC's existing rules. The Commission understands from CFTC staff that entities generally use the CFTC's current certification process if they reasonably believe that the new product does not raise any novel issues or questions. However, the Commission notes that the proposed certification process does not include any final action of the Commission. In cases where a SB SEF desired final agency action, Proposed Rule 808 would be available.[398]

The Commission requests comment on all aspects of Proposed Rule 807. Is the proposed rule text clear? Should a SB SEF be required to include in its certification disclosure of whether a proposed product is or is not subject to mandatory clearing? Should a SB SEF be required to include additional information when certifying a new SB swap product? If so, what additional information should be included? Should the proposed rule enumerate what additional evidence, information or data would need to be provided pursuant to proposed paragraph (a) of Rule 807, or what the time frame for such a request should be? Is the proposed stay of certification process clear? Should the Commission consider adopting another stay procedure? If so, what should that process be?

C. Trading SB Swaps Pursuant to Commission Review and Approval

Proposed Rule 808 would permit a SB SEF to request that the Commission approve a SB swap prior to permitting trading of the SB swap, or if a SB swap product was initially submitted under Rule 807, subsequent to commencement of trading of the SB swap. Under proposed Rule 808, a submission requesting approval would be required to be submitted electronically in a form to be determined by the Commission and include: (1) A copy of the SB swap product's terms and conditions; (2) the documentation relied on to establish the basis for compliance with the Exchange Act and rules and regulations thereunder, including the Core Principles;[399] (3) a written statement verifying that the registered SB SEF has undertaken a due diligence review of the legal conditions, including legal conditions that relate to contractual and intellectual property rights, that may materially affect the trading of the SB swap; (4) if appropriate, a request for confidential treatment as permitted pursuant to the applicable provisions of FOIA[400] and applicable Commission regulations;[401] and (5) a certification that the registered SB SEF has published on its Web site a notice of pending request for approval with the Commission and a copy of the submission, concurrent with the filing of a submission with the Commission.

In addition, under proposed Rule 808(b), if requested by a representative of the Commission, a SB SEF would be required to provide additional evidence, information or data that demonstrates that the SB swap product meets, initially and on a continuing basis, all of the requirements of the Exchange Act and any applicable rules and regulations. Under proposed Rule 808(c) the Commission would approve a new SB swap product unless the terms and conditions of such product were inconsistent with the Exchange Act or rules and regulations thereunder.[402]

Under proposed Rule 808(d), all products submitted for Commission approval under the proposed section would be deemed approved by the Commission 45 days after receipt by the Commission, or at the conclusion of an extended period as provided under proposed Rule 808(e), provided that: (1) The submission complied with the requirements of proposed Rule 808(a); and (2) the SB SEF making the

[395] The stay provision in proposed Rule 807(c) is more similar to the stay provision in proposed Rule 806 and proposed CFTC Rule 40.6 than it is to the stay provision in proposed CFTC Rule 40.2. Proposed CFTC Rule 40.2 would permit the CFTC to stay a certification of a SB swap during the pendency of a CFTC proceeding for filing a false certification or during the pendency of a petition to alter or amend the contract terms and conditions pursuant to Section 8a(7) of the Commodity Exchange Act. The Commission notes that the Exchange Act does not provide for procedures analogous to those in proposed CFTC Rule 40.2, and thus is proposing it to align proposed Rule 807 with proposed CFTC Rule 40.2.

[396] *See* 17 CFR 40.2, 40.3. *See also* 17 CFR 40, Appendix A to Part 40—Guideline No. 1.

[397] *Id.* The Commission understands that the CFTC expect to propose a similar requirement for SEFs.

[398] *See infra* Section XXIV, discussing trading of SB swaps pursuant to Commission review and approval.

[399] *See supra* note 374.

[400] 5 U.S.C. 552.

[401] 17 CFR 200.83.

[402] The standard for approval in proposed Rule 808 would differ from the standard for approval in proposed CFTC Rule 40.3. Proposed CFTC Rule 40.3 provides that the CFTC shall approve a new swap product unless the terms and conditions of such product "violate" the Commodity Exchange Act. *See* 75 FR 67282 (November 2, 2010) (CFTC proposal to amend 17 CFR 40.2–40.5). Notably, proposed CFTC Rule 40.5 provides that the CFTC shall approve an amendment to the terms and conditions of a swap product unless the amended product would be "inconsistent" with the Commodity Exchange Act. *See id.* The Commission believes that it is preferable to have the same standard for approval in proposed Rules 805 and 808 and therefore proposes that the standard for approval in proposed Rule 808 be the same as the standard for proposed CFTC Rule 40.5. The Commission notes that the proposed standard is similar to the standard for Commission approval of a proposed rule change filed under Section 19(b)(2) of the Exchange Act. *See* 15 U.S.C. 78s(b)(2).

submission did not amend the terms and conditions of the proposed SB swap product or supplement its request for approval during that period, except in response to a request by the Commission or for correction of typographical errors, renumbering or other non-substantive revisions. In addition, under proposed Rule 808(d), any voluntary, substantive amendment by the SB SEF would be treated as a new submission.

Under proposed Rule 808(e) the Commission would be able to extend the 45-day review period for an additional 45 days, if the proposed SB swap product raised novel or complex issues that required additional time for review. In that event, the Commission would need to notify the SB SEF within the initial 45 day review period and would need to briefly describe the nature of the specific issues. Alternatively, the SB SEF could agree to any extended review period in writing.

Under proposed Rule 808(f), the Commission could notify the SB SEF at any time during its review of the submission that the Commission will not or is unable to approve the proposed SB swap product. Such notification would be required to specify the nature of the issues raised by the proposed SB swap product and the specific provisions of the Exchange Act rules and regulations involved.

Proposed Rule 808(g) would address the effect of non-approval by the Commission. Under proposed paragraph (g) notification to a SB SEF of the Commission's determination not to approve a proposed SB swap product would not prejudice the SB SEF from subsequently submitting a revised version of the proposed product for Commission approval or from submitting the product as initially proposed pursuant to a supplemented submission. However, notification to a SB SEF of the Commission's refusal to approve SB swap would be presumptive evidence that the entity would not be able to truthfully certify under Rule 807 that the same, or substantially the same, SB swap complies with the Exchange Act or the rules thereunder.

As with proposed Rule 807, proposed Rule 808 is substantially similar to the applicable CFTC proposed rule, new proposed Rule 40.3. The Commission believes that this approach would allow dually registered entities to more easily comply with applicable rules and regulations. The Commission expects that the SB SEF would include in its submission all documentation relied upon to determine that the new product complies with applicable core principles—in particular, core principles that apply specifically to products, such as Core Principle 3 concerning manipulation. The Commission preliminarily believes that it is appropriate to require a SB SEF to document the basis for a determination that a SB swap is not readily susceptible to manipulation and notes that the proposed certification in proposed Rule 808 is drawn from analogous processes that the CFTC currently has in place with respect to new financial futures products proposed to be traded on a designated contract market.[403] The Commission further notes that the CFTC regulations require that prior to trading a new product, a designated contract market must demonstrate that the terms and conditions of a proposed contract "will not be conducive to price manipulation or distortion."[404] The Commission also preliminarily believes that SB SEFs should be conducting due diligence before permitting trading of a new SB swap product. In evaluating any certification, information on such due diligence would be essential to the Commission.

As noted above in the discussion concerning self-certification of new SB swaps, the Commission preliminarily believes that SB SEFs would use the product approval process in instances where they believe novel or difficult issues are presented and they desire final agency action.

The Commission intends to allow registered SB SEFs to submit filings under proposed Rules 807 and 808 electronically through a portal similar to the electronic rule filing system used for proposed rule changes by national securities exchanges and national securities associations.[405] The Commission preliminarily believes that allowing SB SEFs to file new rules and rule amendments in this manner would simplify the filing process and also provide the Commission with prompt access for review. The Commission intends to propose forms for these electronic filings as part of a separate rulemaking.

The Commission requests comment on all aspects of proposed Rule 808. Is the process required by proposed Rule 808 clear? If not, what elements of the process need to be added to the proposed rule? Under what circumstances would a SB SEF that had already certified a new SB swap product request approval of the product pursuant to the proposed rule? Should product approval be mandatory for certain types of SB swaps, as opposed to certification? If so, what products? Please be specific. Is the proposed standard for approval of a SB swap appropriate? If not, why not?

XXV. Discussion of Exemptive Authority Pursuant to Section 36 of the Exchange Act and Compliance Matters

Pursuant to Section 36 of the Exchange Act, the Commission may grant an exemption from any provision of Section 3D of the Exchange Act, any rule or any provision of any rule under Regulation SB SEF, or any provision of the definition of "security-based swap execution facility" in Section 3(a)(77) of the Exchange Act and any Commission rules regarding such definition to the extent that such exemption is necessary or appropriate in the public interest and is consistent with the protection of investors. Any such exemption could be subject to conditions and could be revoked by the Commission at any time. Generally, the Commission would consider entertaining an application for an exemption where the exemption is necessary or appropriate in the public interest and consistent with the protection of investors. The Commission in its sole discretion would determine whether to grant or deny a request for an exemption. In addition, the Commission could revoke an exemption at any time, including if a SB SEF could no longer demonstrate that such exemption is necessary or appropriate in the public interest, or is consistent with the protection of investors.

The Commission requests comment on all aspects of the exemptive authority. Would such exemptive authority be useful to facilitate the purposes of the Dodd-Frank Act? If so, in what circumstances should the Commission grant exemptions? Should exemptions only be granted in limited circumstances? Should the Commission consider granting exemptions from all rules under Regulation SB SEF or are exemptions only warranted for specific rules or specific entities? For example, should exemptions only be available with respect to certain Core Principles? Should the Commission consider granting exemptions from all provisions of Section 3(a)(77) of the Exchange Act, or should exemptions only be available with respect to certain aspects of the definition of "security-based swap execution facility?" What specific factors should the Commission consider in determining whether to grant an exemption? Are there cases where exemptions may not be appropriate and should not be considered?

[403] *See* 17 CFR 40.2, 40.3. *See also* 17 CFR 40, Appendix A to Part 40—Guideline No. 1.

[404] *Id.*

[405] The process for submission of rule filings will be the subject of a separate rulemaking.

The Commission acknowledges that it may take a period of time, as well as require the expenditure of resources, for an SB SEF to implement a number of the requirements set forth in proposed Regulation SB SEF, should those requirements be part of any final rules the Commission may adopt. A potential SB SEF would not be able to determine the final rules governing SB SEFs with which it would need to comply until the Commission adopts those rules. While the Commission is committed to implementing Congress's directive to require SB SEFs to register with the Commission and comply with the Core Principles, the Commission understands that some or all potential SB SEFs may need a period of time in which to acquire or configure the necessary systems, engage and train the necessary staff, and develop and implement the necessary policies and procedures in order to comply with any final rules that the Commission may adopt.

The Commission requests comment as to whether it should provide a SB SEF a certain amount of time to comply with the proposed requirements of Regulation SB SEF applicable to a registered SB SEF once the SB SEF has become registered, and, if so, which provisions, why, and how much time should be provided. For example, proposed Rule 820 relates to the fair representation of participants on the SB SEF's Board. Should the Commission provide for a delayed compliance date for this provision to allow the SB SEF sufficient time to establish the requisite procedures relating to the election of fair representation candidates, including through a petition process, and to align compliance with the date of its election of other directors? [406] Should the Commission consider a delayed compliance date for the CCO's annual report required by proposed Rule 823, for example, if the SB SEF's fiscal year ended shortly after the SB SEF's registration application was approved by the Commission? Are there other proposed rules or provisions of such rules for which a SB SEF should be provided more time to comply after becoming registered? If so, which ones and under what conditions should the Commission permit a delayed compliance date? For example, would it be appropriate to delay the date for an SB SEF to comply with the automated surveillance requirements of proposed Rule 813, as long as the SB SEF had other means to satisfy its surveillance obligations? If so, how long of a delay would be appropriate?

The Commission notes that, under the proposed rules, it would have the authority to temporarily register a SB SEF and, under proposed Regulation SB SEF, a temporarily registered SB SEF would need to comply with Regulation SB SEF, including the rules implementing the Core Principles. Should a phased-in compliance approach apply only with respect to those SB SEFs that are temporarily registered with the Commission? Should phased-in compliance be built into the temporary registration process? Alternatively, should the Commission consider using its Section 36 exemptive authority to exempt SB SEFs from certain of the requirements of Regulation SB SEF on a case-by-case basis? If commenters favor a phased-in compliance approach for certain proposed rules, they should provide specific recommendations, a rationale for each such recommendation, and the conditions under which any such phased-in approach should be granted.

The Commission also seeks comment on whether it is necessary or appropriate for SB SEFs that do not meet certain objective thresholds, such as a trading or volume threshold, to comply with all of the requirements of proposed Regulation SB SEF. To avoid unnecessary barriers to entry that could preclude small SB SEFs from entering this market and better facilitate competition and innovation in the SB swap markets that could be used to promote more efficient trading in organized, transparent and regulated venues, would it be necessary or appropriate to except an SB SEF from certain requirements of proposed Regulation SB SEF under certain conditions, *e.g.,* if the SB SEF does not reach a specified volume or liquidity threshold with respect to the trading of SB swaps. For example, should a SB SEF be excepted from provisions of proposed Rule 816 regarding emergency authority and proposed Rule 822 regarding systems safeguards if the SB SEF does not reach a specified volume or liquidity threshold with respect to the trading of SB swaps? Are there circumstances when it would be burdensome for a SB SEF to undertake electronic surveillance of SB swaps, *e.g.,* if the SB SEF had a low threshold of trading in SB swaps? In that case, would it be appropriate to except the SB SEF from the automated surveillance requirements of proposed Rule 813, as long as the SB SEF had other means to satisfy its surveillance obligations? How should any low volume or other liquidity-based exception be measured, particularly at the outset of trading of SB swaps on registered SB SEFs? Are there other conditions that should be considered in any Commission determination that a SB SEF need not comply with certain provisions of SB SEF and, if so, what are those conditions? In lieu of granting exceptions from certain proposed rules under certain conditions on an omnibus basis, should the Commission instead consider granting exemptions from the provisions of Regulation SB SEF on a case-by-case basis?

XXVI. General Request for Comments

The Commission seeks comment on the proposed interpretation of the definition of SB SEF; creation of a registration framework for SB SEFs; and establishment of rules with respect to the Dodd-Frank Act requirement that a SB SEF must comply with the enumerated fourteen Core Principles and enforce compliance with those principles. The Commission particularly requests comment on possible alternatives to the proposals in this release. The Commission also seeks comments on the general impact the proposals would have on the market for SB swaps.

The Commission invites commenters to address whether the proposed rules are appropriately tailored to achieve the goal of transparency, competition, and efficiency in the SB swap market, including with respect to the administration of the SB SEFs' regulatory activities. The Commission also requests comment on the necessity and appropriateness of mandating the proposed requirements set forth in this release. The Commission seeks comment on the proposals as a whole, including their interaction with the other provisions of the Dodd-Frank Act. The Commission further seeks comment on whether the proposals would help achieve the broader goals of increasing transparency and accountability in the SB swap market.

Commenters should, where possible, provide the Commission with empirical data to support their views. Commenters suggesting alternative approaches should provide comprehensive proposals, including any conditions or limitations that they believe should apply; the reasons for their suggested approaches; and their analysis regarding why their suggested approaches would satisfy the statutory mandate contained in Section 763 of the Dodd-Frank Act.

In considering the proposal, the Commission requests that commenters consider not only each individual proposal contained in proposed Regulation SB SEF but also the totality

[406] *See* Regulation MC Proposing Release, *supra* note 82.

of the Commission's proposals relating to SB SEFs, including the proposed interpretation of the definition of SB SEF, the proposed rules relating to SB SEFs, and the proposed registration requirements for SB SEFs. Do the proposed interpretation of the definition of SB SEF and proposed Regulation SB SEF in their entirety provide an efficient and effective way to implement the requirements of the Dodd-Frank Act relating to SB SEFs? Are the proposed interpretation of the definition of SB SEF and proposed Regulation SB SEF in their entirety properly tailored so that a SB SEF can meet the proposed regulatory requirements and yet be an economically viable business? Are there aspects of the Commission's proposals relating to the regulation of SB SEFs that, when viewed as a whole, are too burdensome, especially in light of the nascent stage of the SB swap market? If so, what are those features and are there ways in which they can be revised? With respect to the proposed rules to implement the Core Principles, commenters are invited to consider, in addition to the costs of each proposed rule, the totality of the costs of all of the proposed rules taken as a whole. Are there any instances in which aspects of the Commission's proposals should not apply? For example, should a system or platform that otherwise would meet the proposed interpretation of the definition of SB SEF, but that does a minimal business in the SB swap market, be exempt from all or some of the requirements of Regulation SB SEF either temporarily or permanently? In general, are there additional steps that the Commission could take that would implement the requirements of the Dodd-Frank Act that apply to SB SEFs and at the same time allow the SB swap market to continue to develop?

Title VII of the Dodd-Frank Act requires that the SEC consult and coordinate to the extent possible with the CFTC for the purposes of assuring regulatory consistency and comparability, to the extent possible,[407] and states that in adopting rules, the CFTC and SEC shall treat functionally or economically similar products or entities in a similar manner.[408]

The CFTC is adopting rules relating to SEFs as required under Section 733 of the Dodd-Frank Act. Understanding that the Commission and the CFTC regulate different products and markets, and as such, appropriately may be proposing alternative regulatory requirements, the Commission requests comments on the impact of any differences between the Commission and CFTC approaches to the regulation of SB SEFs and SEFs. Specifically, do the regulatory approaches under the Commission's proposed rulemaking pursuant to Section 763 of the Dodd-Frank Act and the CFTC's proposed rulemaking pursuant to Section 733 of the Dodd-Frank Act result in duplicative or inconsistent efforts on the part of market participants subject to both regulatory regimes or result in gaps between those regimes? If so, in what ways do commenters believe that such duplication, inconsistencies, or gaps should be minimized? Do commenters believe the approaches proposed by the Commission and the CFTC to regulate SB SEFs and SEFs are comparable? If not, why? Do commenters believe there are approaches that would make the regulation of these facilities more comparable? If so, what are those approaches? Do commenters believe that it would be appropriate for the Commission to adopt an approach proposed by the CFTC that differs from the Commission's proposal? If so, which one? The Commission requests commenters to provide data, to the extent possible, supporting any such suggested approaches.

The Commission seeks comment on whether its proposed rules, either individually or collectively, could permit regulatory arbitrage or have the effect of driving SB swaps and other derivatives transactions to financial centers in other jurisdictions. In this regard, how do the proposed rules compare with comparable existing or proposed rules of other jurisdictions? If the Commission were to adopt the proposed rules, would market participants, end users, and others find it less costly to transact their SB swaps and other derivatives transactions in other jurisdictions? If so, please provide specific details on those jurisdictions that could be regarded as having preferential regulation for trading SB swaps and please identify all the specific rules and circumstances that could lead to such preferences. The Commission also seeks comment on specific actions that it could take to harmonize its proposed rules with those of other jurisdictions consistent with the mandates and goals of the Dodd-Frank Act.

XXVII. Paperwork Reduction Act

Certain provisions of the proposed rules contain new "collection of information" requirements within the meaning of the Paperwork Reduction Act of 1995 ("PRA").[409] The Commission is submitting the proposed collection 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. The title of the new collection of information is Regulation SB SEF. As proposed, Regulation SB SEF would implement the provisions of Title VII of the Dodd-Frank Act relating to the registration and regulation of SB SEFs. Proposed Regulation SB SEF would include rules regarding the registration of a prospective SB SEF on Form SB SEF, rule-writing, reporting, recordkeeping, timely publication of trading information, the filing of new or amended rules or new products with the Commission, reports of the SB SEF's CCO, surveillance systems to capture certain required information and access to SB SEFs by ECPs.[410] 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.

A. Summary of Collection of Information

1. Registration Requirements for SB SEFs and Form SB SEF

A number of the proposed rules under Regulation SB SEF relate to registration with the Commission by an applicant that seeks status as a registered SB SEF. Proposed Rules 801, 802, 803, 804, and proposed Form SB SEF each would contain requirements relating to registration with the Commission by an applicant seeking to register as a SB SEF that would result in a paperwork burden.

Proposed Rule 801(a) would require an applicant to apply for registration with the Commission as a SB SEF by filing electronically, in a tagged data format, a registration application on Form SB SEF in accordance with the instructions contained therein. Under proposed Rule 801(d), an applicant would be required to designate and authorize on Form SB SEF an agent in the United States to accept notice or service of process, pleadings, or other documents in any suit, action or proceedings brought against it to enforce the Federal securities laws or the rules or regulations thereunder. Under

[407] *See* Public Law 111–203, § 712(a)(2).

[408] *See* Public Law 111–203, § 712(a)(7).

[409] 44 U.S.C. 3501 *et seq.*

[410] As proposed, Regulation SB SEF would contain 24 rules that are designated Rule 800 through Rule 823 inclusive; not all of these proposed rules would include a collection of information. The proposed form for registering as a SB SEF under Regulation SB SEF is Form SB SEF. This collection of information includes any collections of information required by proposed Form SB SEF. Unless identified otherwise, all proposed rules referred to in this section would be contained in Regulation SB SEF.

proposed Rule 801(e), an applicant that is controlled by any other person [411] would be required to certify on Form SB SEF and provide an opinion of counsel that any person that controls such SB SEF will consent to and can, as a matter of law, provide the Commission with prompt access to its books and records, to the extent such books and records are related to the activities of the SB SEF, and submit to onsite inspection and examination by representatives of the Commission with respect to the activities of the SB SEF. Under proposed Rule 801(f), a non-resident person applying for registration would be required to certify on Form SB SEF and provide an opinion of counsel that it can, as a matter of law, provide the Commission with prompt access to its books and records and submit to onsite inspection and examination by representatives of the Commission. In addition, proposed Rule 814(b)(4) would require the applicant to certify at the time of registration on Form SB SEF that the SB SEF has the capacity to fulfill its obligations under international information sharing agreements to which it is a party as of the date of such certification.

Proposed Rule 802 relates to amendments to Form SB SEF. Proposed Rule 802(a) would require a SB SEF to file an amendment to Form SB SEF promptly, but in no case later than 5 business days, after the discovery that any information filed on Form SB SEF, any statement therein, or any exhibit or amendment thereto, was inaccurate when filed. Proposed Rule 802(b) would require a SB SEF to file an amendment, on Form SB SEF, within 5 business days after any action is taken that renders inaccurate, or causes to be incomplete, information filed on the Execution Page of the Form SB SEF or as part of Exhibits C, E, G or N,[412] or any amendments thereto. Proposed Rule 802(c) would require a SB SEF that is controlled by any other person to file an amendment to Exhibit P on Form SB SEF within 5 business days after any changes in the legal or regulatory framework of any person that controls the SB SEF that would impact the ability of or the manner in which any such person consents to or provides the Commission prompt access to its books and records, to the extent such books and records relate to the activities of the SB SEF, or impacts the Commission's ability to inspect and examine any such person with respect to the activities of the SB SEF. Proposed Rule 802(d) would require a non-resident SB SEF to file an amendment to Exhibit P on Form SB SEF within 5 business days after any changes in the legal or regulatory framework that would impact the SB SEF's ability to or the manner in which it provides the Commission with prompt access to its books and records or impacts the Commission's ability to inspect and examine the SB SEF. Proposed Rule 802(f) would require a SB SEF to file an annual update to Form SB SEF within 60 days of the end of its fiscal year.

Proposed Rule 803(a) would require a registered SB SEF to provide to the Commission material relating to the trading of SB swaps (including notices, circulars, bulletins, lists, and periodicals) issued or made generally available to SB SEF participants. If the information required to be filed pursuant to proposed Rule 803(a) is available continuously on an Internet Web site controlled by a SB SEF, proposed Rule 803(b) would allow the SB SEF to indicate the location of the Web site where the information may be found and certify that the information available at such Web site is accurate as of its date in lieu of filing such information with the Commission pursuant to proposed Rule 803(a).

Proposed Rule 804(a) would allow a SB SEF to withdraw from registration by filing with the Commission a written notice of withdrawal and an amended Form SB SEF to update any inaccurate information.

Proposed Rules 811(b)(4) and 811(h)(2) would require a SB SEF to report information regarding grants, denials and limitations of access on Form SB SEF and to disclose all disciplinary actions taken annually on its annual update to From SEF, respectively.

2. Rule-Writing Requirements for SB SEFs

A number of the proposed rules under Regulation SB SEF would require a SB SEF to establish rules, policies and procedures with respect to various matters. These are proposed Rules 809(c), 810(b), 811(a)(2), 811(a)(3), 811(b)(1), 811(b)(5), 811(c), 811(d), 811(f), 811(g), 811(i), 813(a), 813(c), 813(d), 814(a), 815(a), 816(a), 816(b), 818(d), 820(a), 820(c) and 822(a)(1).

Proposed Rule 809(c) would require a SB SEF to establish rules setting forth requirements for an eligible person to become a participant in the SB SEF. Such rules would require a participant, at a minimum, to: (1) Be a member of, or have an arrangement with a member of, a registered clearing agency to clear trades in the SB swaps that are subject to mandatory clearing and entered into by the participant on the SB SEF; (2) (i) meet the minimum financial responsibility and recordkeeping and reporting requirements imposed by the Commission by virtue of its registration as a SB swap dealer, major SB swap participant, or broker; or (ii) in the case of an eligible contract participant, meet the recordkeeping and reporting requirements that the SB SEF would establish pursuant to proposed Rule 813; (3) agree to comply with the rules, polices, and procedures of the SB SEF; and (4) consent to the disciplinary procedures of the SB SEF for violations of the SB SEF's rules.

Proposed Rule 810(b) would require a SB SEF to establish: (1) Rules that provide for the equitable allocation of reasonable dues, fees, and other charges among its participants and any other users of its system; (2) rules and systems that are not designed to permit unfair discrimination among participants and any other users of the SB SEF's system; (3) rules that promote just and equitable principles of trade; and (4) rules to provide, in general, a fair procedure for disciplining participants for violations of the rules of the SB SEF.

Proposed Rule 811(a)(2) would require a SB SEF to establish and enforce trading, trade processing, and participation rules that would deter abuses and have the capacity to detect, investigate, and enforce those rules, including means to provide market participants with impartial access to the market and to capture information that may be used in establishing whether rule violations have occurred. Proposed Rule 811(a)(3) would require a SB SEF to establish rules governing the operation of the SB SEF, including rules specifying trading procedures to be used in entering and executing orders traded or posted on the SB SEF, including block trades. Proposed Rule 811(b)(1) would require a SB SEF to establish fair, objective and not unreasonably discriminatory standards for granting impartial access to trading on the SB SEF. Proposed Rule 811(b)(5) would require a SB SEF to establish a fair process for the review of any prohibition or limitation on access with respect to a participant or any refusal to grant access with respect to an applicant. Proposed Rule 811(c) would require a SB SEF to establish rules concerning the terms and conditions of the SB swaps traded on the SB SEF and to have rules stipulating the method by which representation on the swap

[411] *See supra* note 319 and accompanying text regarding the definition of "control."

[412] These Exhibits pertain to the list of officers, directors and committees of the SB SEF (Exhibit C); ownership of the SB SEF (Exhibit E); certain material operating agreements (Exhibit G); and criteria for determining what securities may be traded (Exhibit N).

review committee of the SB SEF shall be chosen by the Board.

Proposed Rule 811(d) would require a SB SEF to establish rules governing the procedures for trading on the SB SEF including, but not limited to: (1) Doing business on the SB SEF; (2) the types of trading interest [413] that would be available on the SB SEF; (3) the manner in which trading interest would be handled on the SB SEF and a requirement for fair treatment of all trading interest; (4) the manner in which price transparency for participants entering trading interest into the system would be promoted; (5) the manner in which trading interest and transaction data would be disseminated, whether to the SB SEF's participants or otherwise, and whether for a fee or otherwise; (6) prohibited trading practices; (7) the prevention of the entry of orders, requests for quotations, responses, quotations, or other trading interest that might result in a trade that is clearly erroneous with respect to the terms of the trade, a fair and non-discriminatory manner of handling any trade that is clearly erroneous, and resolution of any disputes concerning a clearly erroneous trade; (8) trading halts in any SB swap, which rules would be required to include procedures for halting trading in a SB swap when trading has been halted or suspended in the underlying security or securities pursuant to the rules or an order of a regulatory authority with authority over the underlying security or securities; (9) the manner in which block trades would be handled, if different from the handling of non-block trades; and (10) any other rules concerning trading on the SB SEF.

Proposed Rule 811(f) would require a SB SEF to establish rules concerning the reporting of trades executed on the SB SEF to a clearing agency if the transaction is subject to clearing and the procedures for the processing of transactions in SB swaps that occur on or through the SB SEF including, but not limited to, procedures to resolve any disputes concerning the execution of a trade.

Proposed Rule 811(g) would require a SB SEF to establish rules and procedures concerning the disciplining of participants including, but not limited to, rules authorizing its staff to recommend and take disciplinary action for violations of the rules of the SB SEF; specifying the sanctions that may be imposed upon participants for violations of the rules of the SB SEF such that each sanction is commensurate with the corresponding violation; and establishing fair and non-arbitrary procedures for any disciplinary process and appeal thereof.

Proposed Rule 811(i) would require a SB SEF to establish rules and procedures to assure that information to be used to determine whether rule violations have occurred is captured and retained in a timely manner.

Proposed Rule 813(a) would require a SB SEF to establish and enforce rules or terms and conditions defining, or specifications detailing trading procedures to be used in entering and executing orders traded on or through the facilities of the SB SEF and procedures for trade processing of SB swaps on or through the facilities of the SB SEF. Proposed Rule 813(c) would require a SB SEF to establish rules requiring any participant that enters any order or trading interest or executes any transaction on the SB SEF to maintain books and records of any such trading interest or transaction and of any position in any SB swap that is the result of any such trading interest or transaction and to provide prompt access to such books and records to the SB SEF and to the Commission.

Proposed Rule 813(d) would require a SB SEF to establish and maintain procedures to investigate possible rule violations, to prepare reports concerning the findings and recommendations of investigations, and to take corrective action, as necessary.

Proposed Rule 814(a) would require a SB SEF to establish and enforce rules requiring its participants [414] to furnish to the SB SEF, upon request, and in the form and manner prescribed by the SB SEF, any information necessary to permit the SB SEF to perform its responsibilities, including, without limitation, surveillance, investigations, examinations and discipline of participants; such information may include, without limitation, financial information, books, accounts, records, files, memoranda, correspondence, and any other information pertaining to trading interest entered and transactions executed on or through the SB SEF, and to cooperate with and allow access by the SB SEF and representatives of the Commission.

Proposed Rule 815(a) would require a SB SEF to establish and enforce rules and procedures for ensuring the financial integrity of SB swaps entered on or through the facilities of such SB SEF, including the clearance and settlement of SB swaps pursuant to new section 3C(a)(1) of the Exchange Act.

Proposed Rule 816(a) would require a SB SEF to establish rules and procedures to provide for the exercise of emergency authority in consultation or cooperation with the Commission as necessary or appropriate. Proposed Rule 816(b) would require a SB SEF to establish rules and procedures that would specify: (1) The person or persons authorized by the SB SEF to declare an emergency; (2) how the SB SEF would notify the Commission of its decision to exercise its emergency authority; (3) how the SB SEF would notify the public of its decision to exercise its emergency authority; (4) the processes for decision making by the SB SEF personnel with respect to the exercise of emergency authority, including alternate lines of communication and guidelines to avoid conflicts of interest in the exercise of such authority; and (5) the processes for determining that an emergency no longer exists and notifying the Commission and the public of such decision.

Proposed Rule 818(d) would require a SB SEF to establish, maintain, and enforce written policies and procedures to verify the accuracy of the transaction data that it collects and reports.

Proposed Rule 820(a) would require the rules of a SB SEF to assure fair representation of participants in the selection of the SB SEF's Board. Proposed Rule 820(c) would require the rules of a SB SEF to include a fair process for participants to nominate an alternative candidate or candidates to the Board by petition.

Proposed Rule 822(a)(1) would require a SB SEF, with respect to those systems that support or are integrally related to the performance of its activities, to establish, maintain, and enforce written policies and procedures reasonably designed to ensure that its systems provide adequate levels of capacity, resiliency, and security. These policies and procedures would, at a minimum, require the security-based swap execution facility to: (1) Establish reasonable current and future capacity estimates, including quantifying in appropriate units of measure the limits of the SB SEF's capacity to receive (or collect), process, store or display (or disseminate for display or other use) the data elements included within each function, and identifying the factors (mechanical, electronic, or other) that account for the current limitations; (2) conduct periodic capacity stress tests of critical systems to determine such systems' ability to process transactions in an accurate, timely, and efficient

[413] For purposes of this PRA, references to "trading interest" includes any order, request for quotation response, quotation, or any other trading interest on the SB SEF.

[414] *See supra* note 227 and accompanying text regarding the definition of "participant."

manner; (3) develop and implement reasonable procedures to review and keep current its system development and testing methodology; (4) review the vulnerability of its systems and data center computer operations to internal and external threats, physical hazards, and natural disasters, and; (5) establish adequate contingency and disaster recovery plans which shall include plans to resume trading of security-based swaps by the SB SEF no later than the next business day following a wide-scale disruption.

3. Reporting Requirements for SB SEFs

A number of the proposed rules under Regulation SB SEF would require SB SEFs, SB SEF participants and other persons to report or provide information to the Commission or to a SB SEF. Proposed Rules 814, 816(d), 818(a)(3), 818(e), 818(f), 822(a)(2), 822(a)(3), and 822(a)(4) each would contain a reporting requirement.[415] These requirements to report or provide information to the Commission would result in a paperwork burden.

Proposed Rule 814 addresses the ability of a SB SEF to obtain information from its participants, and the ability of Commission representatives to obtain information from a SB SEF and its participants. Proposed Rule 814(a) would require a SB SEF to establish and enforce rules requiring its participants to provide information or documents to the SB SEF upon request. The information or documents requested may include any information that is necessary to permit the SB SEF to perform its regulatory responsibilities, including, without limitation, any financial information, books, accounts, records, files, memoranda, correspondence, and any other information pertaining to trading interest entered and transactions executed on or through the SB SEF. Proposed Rule 814(a) also would direct a SB SEF to require its participants to allow access by any Commission representative to examine the participant's books and records and to obtain or verify information related to trading interest entered or transactions executed on or through the SB SEF.[416] Proposed Rule 814(b) would direct a SB SEF to allow access by any Commission representative to examine the SB SEF's books and records and to obtain or verify information related to trading interest entered or transactions executed on or through the SB SEF. Proposed Rule 814(b)(3) would require a SB SEF to have the capacity to carry out such international information-sharing agreements as the Commission may require.

Proposed Rule 816(d) would require a SB SEF to notify the Commission promptly of any exercise of its emergency authority, and within two weeks following cessation of an emergency, submit to the Commission a report explaining the basis for declaring an emergency, how conflicts of interest were minimized in the SB SEF's exercise of its emergency authority, and the extent to which the SB SEF considered the effect of its emergency action on the markets for the SB swap and any security or securities underlying the SB swap.

Proposed Rule 818 would establish both recordkeeping and reporting obligations for SB SEFs. Proposed Rule 818(e) would require a SB SEF to report to the Commission such information as the Commission may, from time to time, determine to be necessary to perform the duties of the Commission under the Exchange Act. Proposed Rule 818(f) would require a SB SEF to provide to any representative of the Commission, upon request, copies of documents required to be kept and preserved pursuant to the recordkeeping requirements of proposed Rules 818(a) and (b).

Proposed Rule 822 addresses system safeguards for the SB SEF. Proposed Rule 822(a)(2) would require a SB SEF to submit to the Commission on an annual basis an objective review with respect to those systems that support or are integrally related to the performance of the SB SEF's activities. If the objective review is performed by an internal department, an objective, external firm would be required to assess the internal department's objectivity, competency, and work performance. Proposed Rule 822(a)(3) would require a SB SEF to promptly notify the Commission in writing of material systems outages and any remedial measures implemented or contemplated and submit to the Commission within five business days of when the outage occurred a written description and analysis of the outage and any remedial measures that have been implemented or are contemplated. Proposed Rule 822(a)(4) would require a SB SEF to notify the Commission in writing at least thirty calendar days before implementation of any planned material systems changes.

4. Recordkeeping Required Under Regulation SB SEF

Proposed Rule 818(a) would require a SB SEF to keep and preserve at least one copy of all documents, including all correspondence, memoranda, papers, books, notices, accounts, and other such records, including the audit trail records required pursuant to proposed Rule 818(c), as shall be made and received in the conduct of its business. Proposed Rule 818(b) would require SB SEFs to keep and preserve such documents and other records for a period of not less than five years, the first two years in an easily accessible place. Proposed Rule 818(c) would require SB SEFs to establish and maintain accurate, time-sequenced records of all trading interest and transactions received by, originated on, or executed on the SB SEF. In addition, proposed Rule 811(b)(3) would require that a SB SEF make and keep records relating to all grants of access and the basis for such grant, and all denials or limitations of access to the SB SEF and the reasons for such denial or limitation. Proposed Rule 811(h) would require a SB SEF to make and keep records relating to all disciplinary proceedings, sanctions imposed, and appeals thereof.[417]

5. Timely Publication of Trading Information Requirement for SB SEFs

Proposed Rule 817(a)(1) would require a SB SEF to have the capacity to electronically capture, transmit, and disseminate information on price, trading volume, and other trading data on all SB swaps executed on or through the SB SEF.[418]

[415] In addition, proposed Rule 823 would require the SB SEF's CCO to submit to the Commission an annual compliance report, along with a financial report. The paperwork burden associated with the CCO's reports, including for proposed Rules 811(b)(4) and 811(g), and 814(b) that set forth certain items to be addressed in the CCO's reports, is addressed separately in Section XXVII.A.7., below.

[416] The Commission notes that proposed Rule 813(c)(2) similarly requires a SB SEF to establish and enforce rules that require any participant that enters any trading interest or executes any transaction on the SB SEF to provide the Commission with prompt access to its books and records. The Commission considers the prompt access requirement of proposed Rule 813(c)(2) to be included in the burden estimates of proposed Rule 814(a) for purposes of this PRA analysis.

[417] The records required by proposed Rules 811(b)(3) and 811(g) would be included in the business records required to be kept pursuant to proposed Rule 818. Therefore, the Commission preliminarily believes that the paperwork burden for these rules would be included in the estimated burden for proposed Rule 818. *See infra* note 493 and accompanying text.

[418] Proposed Rule 817(a)(2) requires every SB SEF to make public timely information on price, trading volume, and other trading data on SB swaps to the extent required by the Commission. The Commission notes that proposed Rule 817(a)(2) does not require a SB SEF to make public timely information on price, trading volume, and other trading data on SB swaps. Rather, the Commission has proposed that other parties be responsible for timely publication of trading information. *See* Reporting and Dissemination Release *supra* note 6.

6. Rule Filing and Product Filing Processes for SB SEFs

Proposed Rules 805 and 806 relate to the submission to the Commission of filings of new or amended rules, while proposed Rules 807 and 808 relate to the submission to the Commission of filings to make SB swap products available to trade. Proposed Rules 805, 806, 807, and 808 would impose a collection of information burden on SB SEFs.[419]

Rule Filings: Proposed Rules 805 and 806 would require a SB SEF to submit rule filings for new rules or rule amendments, including changes to an existing product's terms or conditions.[420] Under proposed Rules 805(a) and 806(a), a SB SEF could submit either a voluntary request for prior approval or a self-certified rule filing, respectively, for any new rules or rule amendments. Under both proposed rules, a SB SEF would be required to submit the rule filings electronically to the Commission in a format to be specified by the Commission.[421] Both proposed Rules 805(a) and 806(a) would require the SB SEF to include the following information in the requisite rule filings: (1) The text of the proposed rule or rule amendment (in the case of a rule amendment, deletions and additions would need to be indicated); (2) the proposed effective date or intended date of implementation, as applicable; (3) the documentation relied on by the SB SEF to establish the basis for compliance with the applicable provisions of the Exchange Act and the rules and regulations thereunder (including Section 3D(d) of the Exchange Act and the rules and regulations thereunder); (4) a certification or written statement, as applicable, that the SB SEF has published a notice of pending new rule or rule amendment, or a notice of pending certification, as applicable, on the SB SEF's Web site and a copy of the submission, concurrent with its filing with the Commission; (5) a description of any substantive opposing views on the rule that were expressed to the SB SEF by the Board or committee members, participants or market participants that were not incorporated into the rule (or, with respect to a self-certification filing under Rule 806(a), a statement that no such opposing views were expressed, if applicable); (6) a request for confidential treatment, if appropriate; and (7) for proposed amendments to a product's terms and conditions, a written statement that the SB SEF has undertaken a due diligence review of the legal conditions, including conditions relating to contractual and intellectual property rights, that may materially affect the trading of the product.

In addition, for voluntary requests for prior approval rule filings, proposed Rule 805(a) would also require SB SEFs to include: (1) A description of any action taken or anticipated to be taken to adopt the proposed rule by the SB SEF or its Board, or by any committee thereof, and a citation to the rules of the SB SEF that authorize the adoption of the proposed rule change; (2) an explanation of the operation, purpose and effect of the proposed new rule or rule amendment, including, as applicable, a description of the anticipated benefits to market participants or others, any potential anticompetitive effects on market participants or others, and how the rule fits into the SB SEF's framework of regulation; (3) any additional information that may be beneficial to the Commission in analyzing the new rule or rule amendment (and if the proposed rule affects, directly or indirectly, the application of any other rule of the SB SEF, the pertinent text of any such rule must be set forth and the anticipated effect described); and (4) and the identification of any Commission rule or regulation that Commission may need to amend or interpret in order to approve the new rule or rule amendment and, to the extent that such an amendment or interpretation is necessary to accommodate the new rule or rule amendment, a reasoned analysis supporting the proposed amendment or interpretation.

For self-certification rule filings, proposed Rule 806(a) also would require a SB SEF to include: (1) A certification by the SB SEF that the rule complies with the Exchange Act and Commission rules and regulations thereunder; and (2) upon request of any representative of the Commission, additional evidence, information, or data that may be beneficial to the Commission in conducting a due diligence assessment of the filing and the SB SEF's compliance with any of the requirements of the Exchange Act or the rules and regulations thereunder.

Product Filings: Proposed Rules 807 and 808 would require a SB SEF to submit product filings prior to trading a SB swap. Under proposed Rules 807(a) and 808(a), a SB SEF could submit either a self-certified product submission or voluntary request for prior approval product filing, respectively, before trading a SB swap. Under both proposed rules, a SB SEF would be required to submit the product filings electronically to the Commission in a format specified by the Commission. Both proposed Rules 807(a) and 808(a) would require SB SEFs to include the following information in the product filings: (1) A copy of the SB swap's terms and conditions, (2) the documentation relied on to establish the basis for compliance with the Exchange Act and rules and regulations thereunder (including Section 3D(d) of the Exchange Act and the rules and regulations thereunder); (3) a written statement verifying that the SB SEF has undertaken a due diligence review of the legal conditions, including legal conditions that relate to contractual and intellectual property rights, that may materially affect the trading of the SB swap; (4) a request for confidential treatment, if appropriate; and (5) a certification that the SB SEF has published on its Web site a notice of pending request for approval, or a notice of pending certification, as applicable, and a copy of the submission, concurrent with the filing of the submission with the Commission. In addition, for self-certification product filings, proposed Rule 807(a) also would require a SB SEF to include the following information: (1) The intended date on which the SB swap may begin trading, and (2) a certification by the SB SEF that the SB swap to be traded complies with the Exchange Act and the rules and regulations thereunder, including Section 3D(d) of the Exchange act and the rules and regulations thereunder.

In addition, proposed Rules 807(b) and 808(b) would require a SB SEF to provide, upon request of any representative of the Commission, additional evidence, information, or data that demonstrates that the SB swap meets, initially or on a continuing basis, all of the requirements of the Exchange Act and rules and regulations thereunder.

7. Requirements Relating to the SB SEF's Chief Compliance Officer

Proposed Rule 823 addresses the obligations of the SB SEF's CCO, including the CCO's performance of his or her statutory duties with respect to the SB SEF and its statutory

[419] The Commission expects to conduct a separate rulemaking that would propose the form for the electronic submission of such filings to the Commission and the procedures pertinent to such form. Should the Commission propose any such form and associated procedures, it would include a collection of information burden as part of that proposed rulemaking.

[420] Filings that relate to proposed changes to an existing SB swap's terms or conditions would be submitted under proposed Rules 806 or 807.

[421] *See supra* Section XXIII.

requirement to prepare and submit to the Commission annual compliance and financial reports.

Proposed Rule 823(a) would require the SB SEF's Board to designate a CCO to perform the duties identified in proposed Rule 823(b) through (e). Under proposed Rule 823(b)(6) and (7), the CCO would be responsible for establishing procedures for the remediation of noncompliance issues identified by the CCO identified through any compliance office review, look-back, internal or external audit finding, self-reported error or validated complaint, and establishing appropriate procedures for the handling, management response, remediation, retesting, and closing of noncompliance issues.

The CCO also would be required under proposed Rule 823(c) and (d) to prepare and submit annual compliance reports to the Commission and the SB SEF's Board containing, at a minimum: (1) A description of the SB SEF's enforcement of its policies and procedures; (2) information on all investigations, inspections, examinations, and disciplinary cases opened, closed, and pending during the reporting period; (3) all grants of access (including, for all participants, the reasons for granting such access) and all denials or limitations of access (including for each applicant, the reasons for denying or limiting access), consistent with proposed Rule 811(b)(3); (4) any material changes to the policies and procedures since the date of the preceding compliance report; (5) any recommendation for material changes to the policies and procedures as a result of the annual review, the rationale for such recommendation, and whether such policies and procedures were or will be modified by the SB SEF to incorporate such recommendation; (6) the results of the SB SEF's surveillance program, including information on the number of reports and alerts generated, and the reports and alerts that were referred for further investigation or for an enforcement proceeding; (7) any complaints received regarding the SB SEF's surveillance program; and (8) any material compliance matters identified since the date of the preceding compliance report.

The CCO is required under proposed Rule 823(e)(1) and (2) to submit annually a financial report for the SB SEF and for certain affiliated entities of the SB SEF. Among other things, the annual financial report for the SB SEF must be audited by a registered public accounting firm that is qualified and independent in accordance with Rule 2–01 of Regulation S–X (17 CFR 210.2–01), be a complete set of financial statements of the SB SEF that are prepared in accordance with U.S. generally accepted accounting principles for the two most recent fiscal years of the SB SEF. For certain affiliated entities (every subsidiary in which the applicant has, directly or indirectly, a 25% interest and for every entity that has, directly or indirectly, a 25% interest in the applicant), the SB SEF must provide a financial report consisting of a complete set of unconsolidated financial statements (in English) for the latest two fiscal years and include such footnotes and other disclosures as are necessary to avoid rendering the financial statements misleading. As proposed, the reports for the SB SEF and for the SB SEF's affiliated entities would be provided in XBRL consistent with Rules 405(a)(1), (a)(3), (b), (c), (d) and (e) of Regulation S–T.[422] The Commission notes that these annual financial reports are the same as those required to be produced upon registration and annually pursuant to Exhibits F and H to proposed Form SB SEF for the SB SEF. In addition, pursuant to Exhibit H to proposed Form SB SEF, the Commission may request unaudited financial information for any other affiliated entity not covered by the 25% interest threshold discussed above.

8. Surveillance Systems Requirements for SB SEFs

Several proposed rules under Regulation SB SEF would require a SB SEF to electronically surveil its market and to maintain an automated surveillance system. To the extent that such surveillance and systems would require a SB SEF to collect and assess data and other information, such rules would result in a collection of information.

Proposed Rule 811(j) would require a SB SEF to have the capacity to capture information that may be used in establishing whether rule violations have occurred, including through the use of automated surveillance systems as set forth in proposed Rule 813(b). Proposed Rule 813(a)(2) would require a SB SEF to monitor trading in SB swaps to prevent manipulation, price distortion, and disruptions of the delivery or cash settlement practices and procedures, including methods for conducting real-time monitoring of trading and comprehensive and accurate trade reconstructions. Proposed Rule 813(b) would require a SB SEF to have the capacity and appropriate resources to electronically monitor trading in SB swaps on its market by establishing an automated surveillance system, including through real-time monitoring of trading and use of automated alerts.[423]

9. Access by Non-Registered Eligible Contract Participants

Proposed Rule 809(d)(1) would require a SB SEF that provides direct access to non-registered ECPs as participants to establish, document, and maintain a system of risk management controls and supervisory procedures reasonably designed to manage the financial, regulatory, and other risks of this business activity.[424] Proposed Rule 809(d)(2) would require that the risk management controls and supervisory procedures for granting access to ECPs as participants of the SB SEF to be reasonably designed to ensure compliance with all regulatory requirements.[425]

10. Composite Indicative Quote and Executable Bids and Offers

Proposed Rule 811(e) would require a SB SEF that operates an RFQ platform to create and disseminate through the SB SEF a composite indicative quote, made available to all participants, for SB swaps traded on or through the SB SEF. The Commission's proposed interpretation of SB SEF would require each SB SEF, at the minimum, to provide any participant with the ability to make and display executable bids or offers accessible to all participants on the SB SEF, if the participant wishes to do so.

B. Proposed Use of Information

1. Registration Requirements for SB SEFs and Form SB SEF

As discussed above, proposed Rules 801, 802, 803 and 804 would require an applicant to register on Form SB SEF, file certain amendments and updates to Form SB SEF, file other supplemental information with the Commission with respect to the trading of SB swaps, and provide notice to the Commission of the SB SEF's withdrawal of registration. The information collected pursuant to these proposed rules would enhance the ability of the Commission to determine whether to approve the registration of an entity as a SB SEF; to monitor and oversee SB SEFs; to determine that SB

[422] *See* 17 CFR 232.405.

[423] The collection of information burdens associated with the audit trail provisions of proposed Rule 818(a) and (c) are discussed in the sections of this PRA analysis relating to recordkeeping.

[424] *See* proposed Rule 809(d)(1). Non-registered ECPs are eligible contract participants that are not registered with the Commission as a SB swap dealer, major SB swap participant, or broker (as defined in section 3(a)(4) of the Exchange Act).

[425] *See* proposed Rule 809(d)(2).

SEFs initially comply, and continue to operate in compliance, with the Exchange Act, including the Core Principles applicable to SB SEFs, and the rules and regulations thereunder; to carry out its statutorily mandated oversight functions; and to maintain accurate and updated information regarding SB SEFs. Because the registration information would be publicly available, it could also be useful to SB SEF's participants, other market participants, other regulators, and the public generally.

2. Rule-Writing Requirements for SB SEFs

The proposed provisions of Regulation SB SEF requiring that SB SEFs establish certain rules, policies and procedures would help SB SEFs comply with the Exchange Act, including the Core Principles applicable to SB SEFs, and the rules and regulations thereunder. The rules also would be useful to the SB SEF's participants in understanding and complying with the requirements of the SB SEF and to other market participants, other regulators, and the public generally.

3. Reporting Requirements for SB SEFs

The information that would be collected under the proposed provisions of Regulation SB SEF requiring SB SEFs, SB SEF participants, and other persons to submit certain reports and provide certain information upon request would be used by the Commission to assist in its oversight of SB SEFs and the SB swap markets.

4. Recordkeeping Required Under Regulation SB SEF

Proposed Rule 813(c) would aid the SB SEF in detecting and deterring fraudulent and manipulative acts with respect to trading on its market, as well as help it to fulfill the statutory requirement in Core Principle 4 that a SB SEF monitor trading in SB swaps, including through comprehensive and accurate trade reconstructions. The proposed rule also would aid the Commission in carrying out its responsibility to oversee SB SEFs.

Proposed Rules 818(a) and (b) would help to ensure that records exist, and thus would be available to the Commission pursuant to the proposed reporting requirements. Access to these records would provide a valuable tool to help the Commission carry out its oversight responsibility over SB SEFs and the SB swap markets in general.

The audit trail information required to be maintained under the proposed Rule 818(c) would facilitate the ability of the SB SEF and the Commission to carry out their respective obligations under the Exchange Act, by providing a record of the complete history of all trading interest entered and transactions executed on the SB SEF, which data could be used to help detect abusive or manipulative trading activity, prepare reconstructions of activity on the SB SEF or in the SB swaps market, and generally to understand the causes of unusual market activity. In addition, proposed Rule 811(b)(3) would require every SB SEF to make and keep records of all grants, denials, or limitations of access to the SB SEF, which would provide the Commission an important tool to help it assess whether the SB SEF is meeting its duty to provide fair and impartial access to its facility. Further, proposed Rule 811(h) would require the SB SEF to make and keep records specifically of all disciplinary proceedings and appeals, which would allow the Commission to review the disciplinary process at a SB SEF and would provide the Commission an additional tool to carry out its oversight responsibilities.

5. Timely Publication of Trading Information Requirement for SB SEFs

The requirement contained in proposed Rule 817 that a SB SEF have the capacity to electronically capture, transmit, and disseminate information on price, trading volume, and other trading data on all SB swaps executed on or through the SB SEF, would assist the SB SEF in carrying out its regulatory responsibilities under the Exchange Act, including, without limitation, the proposed requirements that every SB SEF must keep and preserve books and records of activities related to its business, and allow access by the Commission to obtain or verify other information related to orders entered and transactions executed on or through the SB SEF's facilities. In addition, the Commission believes that every SB SEF must have the capacity to capture this information to enable the SB SEF to comply with reasonable requests to provide information to others, including, SB SEF participants, counterparties, registered SDRs, or regulatory authorities.

6. Rule Filing and Product Filing Processes for SB SEFs

Proposed Rules 805 and 806 would require a SB SEF to submit new rule or rule amendments as rule filings either through a voluntary prior approval process or a self-certification process. The information that would be collected under these proposed rules would help ensure compliance by the SB SEF with the provisions of the Exchange Act, including the Core Principles applicable to SB SEFs, and the rules and regulations thereunder, as well as assist the Commission in overseeing the SB SEF's compliance with its regulatory obligations. This information also would be useful to the SB SEF's participants, because they would be subject to such new or amended rules and thus would have an interest in learning about those rules and potentially in submitting to the Commission comments on any proposed new or amended rules. Other market participants, other SB SEFs, and other regulators, as well as the public generally, may find information about proposed new or amended rules useful.

Proposed Rules 807 and 808 would require a SB SEF to submit filings for new products that they make available for trading either through a self-certification process or a voluntary prior approval process. The information that would be collected under these proposed rules would help ensure that any SB swap that is available to trade on the SB SEF would comply with the provisions of the Exchange Act, including the Core Principles applicable to SB SEFs, and the rules and regulations thereunder, as well as assist the Commission in overseeing the SB SEF's compliance with its regulatory obligations. In particular, the requirements of proposed Rules 807(a) and 808(a) should help the Commission determine the SB SEF's compliance with the Core Principles that apply specifically to products, such as Core Principle 3 which would require a SB SEF to ensure that a SB swap trading on its facility is not readily susceptible to manipulation. Other market participants, other SB SEFs, and other regulators, as well as the public generally, may find information about the new products useful.

7. Requirements Relating to the SB SEF's CCO

As discussed above, proposed Rule 823 would require that a SB SEF's CCO establish certain policies relating to noncompliance issues as well as prepare and submit to the Commission both an annual compliance report and an annual financial report. The information that would be collected under this proposed rule would help ensure compliance by SB SEFs with the provisions of the Exchange Act, including the Core Principles applicable to SB SEFs, and the rules and regulations thereunder, as well as assist the Commission in overseeing the SB SEFs. The Commission could use the annual compliance report to help it evaluate

whether the SB SEF is carrying out its statutorily-mandated regulatory obligations and, among other things, to discern the scope of any denials of access or refusals to grant access by the SB SEF and to obtain information on the status of the SB SEF's regulatory compliance program. The annual financial report would provide the Commission with important information on the financial health of the SB SEF.

8. Surveillance Systems Requirements for SB SEFs

The proposed rules requiring a SB SEF to maintain certain surveillance systems and monitor trading would enable the SB SEFs to have the capacity and resources to fulfill its obligations under the Exchange Act to oversee trading on its market, and to prevent manipulation and other unlawful activity or disruption of the market. These systems would help the SB SEF to identify and investigate market behavior that may be improper and bring any necessary disciplinary actions.

9. Access by Non-Registered Eligible Contract Participants

Proposed Rule 809 would permit a SB SEF to provide access to the SB SEF by non-registered ECPs, provided that the conditions of the proposed rule relating to such access would be satisfied. Proposed Rule 809(d) would require a SB SEF that would permit access to non-registered ECPs [426] to establish, document, and maintain a system of risk management controls and supervisory procedures reasonably designed to manage the financial, regulatory, and other risks of this business activity. The risk management controls and supervisory procedures for granting access to non-registered ECPs would be required to be reasonably designed to ensure compliance with all regulatory requirements. Since non-registered ECPs are not directly subject to capital or other financial requirements, there is a concern that, in the absence of risk management controls and supervisory procedures, they could enter into trades that exceed appropriate capital or credit limits. The proposal relating to risk management controls and supervisory procedures is intended to help manage these risks associated with allowing non-registered ECPs to have direct access to an SB SEF's market.

10. Composite Indicative Quote and Executable Bids and Offers

As discussed above, proposed Rule 811(e) would require a SB SEF that operates an RFQ platform to create and disseminate through the SB SEF a composite indicative quote, made available to all participants, for SB swaps traded on or through the SB SEF. The Commission preliminarily believes that a composite indicative quote would provide a certain level of pre-trade transparency for an RFQ platform. In addition, the Commission's proposed interpretation of SB SEF would require each SB SEF, at the minimum, to provide any participant with the ability to make and display executable bids or offers accessible to all participants on the SB SEF, if the participant wishes to do so. The Commission preliminarily believes that this functionality would provide greater access to the SB SEF for participants.

C. Respondents

The collection of information associated with the proposed Regulation SB SEF would apply to entities seeking to register as, and to registered, SB SEFs. In the Dodd-Frank Act, Congress incorporated into the Exchange Act a definition of SB SEF and mandated the registration and regulation of these new facilities.[427] There currently are no registered SB SEFs. Based on conversations with the CFTC and industry sources, the Commission preliminarily believes that approximately 10 to 20 entities could seek to register as SB SEFs and thus be subject to the collection of information requirements of these proposed rules. The Commission is using the higher estimate of 20 SB SEFs for this PRA analysis.[428]

In addition, proposed Rules 813(c) and 814(a) would impose collection of information burdens on SB SEF participants. Based on conversations with industry sources, the Commission preliminarily believes that there could be a total of 275 persons that could become SB SEF participants and would thus be subject to the collection of information requirements of the proposed rules.[429]

Except with regard to the collection of information burdens imposed on SB SEF participants pursuant to proposed Rules 813(c) and 814(a), as discussed further in the sections of this PRA discussing the reporting and recordkeeping requirements of Regulation SB SEF, the respondents subject to the collection of information burdens associated with proposed Regulation SB SEF would be SB SEFs.

D. Total Annual Reporting and Recordkeeping Burden

1. Registration Requirements for SB SEFs and Form SB SEF

Initial filings on Form SB SEF by a prospective SB SEF seeking to register with the Commission pursuant to proposed Rule 801 would be made on a one-time basis. As discussed above, no SB SEFs currently are registered with the Commission and the Commission preliminarily estimates that 20 entities initially would seek to register with the Commission as SB SEFs. The Commission's estimate regarding the initial burden that a SB SEF would incur to file a Form SB SEF is informed by its estimate of the number of hours necessary to complete a Form 1 for registration of a national securities exchange. The Commission calculated in 2010 that Form 1 takes 47 hours to complete.[430] Although the requirements of Form 1 are not identical to the requirements of proposed Form SB SEF, the Commission preliminarily believes that they are substantially similar for PRA purposes. Similar to Form 1, the information that would be required on Form SB SEF generally would consist of copies of existing documents that would be prepared by a SB SEF in the ordinary course of its business. As noted above, no SB SEFs currently are registered with the Commission and no framework for registration of SB SEFs currently exists. Therefore, the Commission preliminarily believes that, during the initial implementation period of

[426] *See* proposed Rule 809.

[427] *See* Public Law 111–203, § 761(a) (adding Section 3(a)(77) of the Exchange Act), defining the term "security-based swap execution facility." *See also* Public Law 111–203, § 763(c) (adding Section 3D of the Exchange Act).

[428] This estimate comports with the estimated number of SB SEFs contained in the Regulation MC Proposing Release, *supra* note 82.

[429] 275 = 50 (estimated number of SB swap dealers that would be SB SEF participants) + 5 (estimated number of major SB swap participants that would be SB SEF participants) + 10 (estimated number brokers that would be SB SEF participants) + 210 (estimated number of ECPs that would be SB SEF participants). The Commission recently proposed rules to define a number of terms used in Title VII, including, among others, "security-based swap dealer" and "major security-based swap participant." *See* Securities Exchange Act Release No. 63452 (December 7, 2010), 75 FR 80174 (December 21, 2010). As part of that proposal, the Commission preliminarily estimated that approximately 50 entities may be required to register as SB swap dealers under the proposed rules. *See* 75 FR at 80209 n.188. The Commission further estimated that no more than ten entities would have SB swap positions large enough that they would have to monitor whether they meet the thresholds defining a major SB swap participant. *See* 75 FR at 80207–08. For purposes of these proposed rules, the Commission conservatively assumes that there would be a total of five major SB swap participants, while recognizing that in fact there may be fewer than five.

[430] *See* 75 FR 32824 (June 9, 2010) (outlining the most recent Commission calculations regarding the PRA burdens for Form 1 and Rules 6a-1 and 6a-2 under the Exchange Act).

Regulation SB SEF, it could take a SB SEF more time to compile the necessary documents and information required by the exhibits to Form SB SEF than it would for an applicant to become a national securities exchange to compile documents and information to comply with requirements of Form 1. The procedures for registration as a national securities exchange are well-settled and, therefore, an entity that intends to register as national securities exchange could anticipate the form of the documents and other information that it would need to compile to register on Form 1.[431] Based on these factors, the Commission preliminarily estimates that an applicant would incur an average burden of 100 hours to prepare and file an initial Form SB SEF, including all exhibits thereto, except Exhibits F and H requiring certain financial reports, and Exhibit P requiring certain opinions of counsel, which are discussed separately below.[432] Therefore, the Commission preliminarily estimates that the aggregate one-time burden for all respondents to file the initial Form SB SEF, including all exhibits thereto, except Exhibits F and H requiring certain financial reports and Exhibit P requiring opinions of counsel, would be 2,000 hours.[433] The Commission preliminarily believes that SB SEFs would prepare Form SB SEF internally. The Commission requests comment on the accuracy of this estimate.

Exhibits F and H to proposed Form SB SEF would require an applicant to submit an annual financial report that would have to satisfy a number of requirements, including the requirement that a registered public accounting firm that is qualified and independent in accordance with Rule 2–01 of Regulation S–X[434] audit each financial report relating to the SB SEF (unaudited for certain affiliated entities). The Commission preliminarily believes that it is unlikely that, during the initial implementation period of Regulation SB SEF, a SB SEF would have prepared such reports in the ordinary course of business prior to applying for registration on Form SB SEF. Therefore, in connection with its efforts to register as a SB SEF with the Commission on proposed Form SB SEF, an applicant would incur an initial burden to generate such financial reports. Based on conversations with operators of current trading platforms and the Commissions experience with entities of similar size, the Commission preliminarily estimates that the financial reports relating to the SB SEF would generally require, on average, 500 hours per respondent to complete and cost $500,000 for independent public accounting services per respondent.

The Commission believes that the unaudited reports required for certain affiliated entities and to be made available upon request by the Commission for other affiliated entities would not be overly time consuming to produce because, based on the Commission's experience with Form 1 filers, a respondent's accounting system should have this information available. Furthermore, because the information would not have to be audited, a respondent would be able to compile the required information using a computer and commercially available software that it generally would own for pre-existing accounting purposes and then would submit the information to the Commission. Based on the number of unaudited financial statements the Commission receives from filers of Form 1 and the substance contained in these reports, the Commission estimates that it would take 40 hours to compile, review, and submit these reports.

However, as proposed, all of these reports would be required to be provided in XBRL, as required in Rules 405(a)(1), (a)(3), (b), (c), (d) and (e) of Regulation S–T.[435] This would create an additional burden on respondents. The Commission preliminarily estimates, based on its experience with other data tagging initiatives, that these requirements would add an additional burden of an average of 54 hours and $23,000 in outside software and other costs per respondent. Thus, for complying with the financial statement requirements under Exhibits F and H in connection with an initial application on proposed Form SB SEF, the Commission estimates an aggregate total initial burden of 11,880 hours[436] and $10,460,000 for all respondents.[437] The Commission solicits comments as to the accuracy of these estimates.

Pursuant to the requirements of proposed Rule 801(e), Exhibit P to proposed Form SB SEF would require an applicant that is controlled by any other person to provide an opinion of counsel that any person that controls such SB SEF has consented to and can, as a matter of law, provide the Commission with prompt access to its books and records, to the extent such books and records are related to the activities of the SB SEF, and submit to onsite inspection and examination by representatives of the Commission with respect to the activities of the SB SEF. This creates an additional burden for SB SEFs controlled by other persons. Based on similar requirements on Form 20–F, the Commission preliminarily estimates that this additional burden would add 1 hour and $900 in outside legal costs for each affected SB SEF.[438] For PRA

[431] For example, because an entity seeking to register as a national securities exchange would know that Exhibit E to Form 1 requires an applicant to describe the manner and operation of the electronic trading system to be used to effect transactions on the exchange, such entity likely would prepare such a description in the ordinary course of its business in anticipation of applying for registration as a national securities exchange on Form 1. However, because the requirements of Form SB SEF would be set forth for the first time in connection with this proposed rulemaking, a SB SEF previously may not have prepared a description of the manner and operation of its trading system in the ordinary course of business and would have to do so to comply with Exhibit I to Form SB SEF.

[432] As discussed above, proposed Rule 801(d) would require a SB SEF to designate and authorize on Form SB SEF an agent in the U.S. to accept notice or service of process, pleadings, or other documents in any action or proceedings brought against it to enforce the Federal securities laws and the rules and regulations thereunder. Proposed Rule 801(e) would require an applicant that is controlled by any other person to certify on Form SB SEF that any person that controls such SB SEF would consent to and could, as a matter of law, provide the Commission with prompt access to its books and records, to the extent such books and records are related to the activities of the SB SEF, and submit to onsite inspection and examination by representatives of the Commission with respect to the activities of the SB SEF. Proposed Rule 801(f) would require a non-resident person applying for registration to certify on Form SB SEF that it could, as a matter of law, provide the Commission with prompt access to its books and records and submit to onsite inspection and examination by representatives of the Commission. Proposed Rule 814(b)(4) would require a SB SEF to certify at the time of registration on Form SB SEF that the SB SEF would have the capacity to fulfill its obligations under international information sharing agreements to which it is a party. The Commission preliminarily believes that the burden associated with these requirements would be included in the 100-hour burden associated with the initial registration on Form SB SEF required by proposed Rule 801(a). These proposed requirements currently are not included on Form 1. In addition, proposed Rules 801(e) and (f) would require SB SEFs that are controlled by other persons and non-resident SB SEFs to provide certain opinions of counsel. The Commission preliminarily believes that the burden associated with these requirements would be included in the burden associated with Exhibit P to Form SB SEF discussed below.

[433] 2,000 hours = 20 (number of SB SEF respondents) x 100 hours (initial hourly burden to comply with Form SB SEF, except for Exhibits F, H and P).

[434] *See* 17 CFR 210.2–01.

[435] *See* 17 CFR 232.405.

[436] 11,880 hours = 20 (number of SB SEF respondents) × 594 hours (500 hours for audited SB SEF financial statements + 40 hours for unaudited financial statements of affiliated entities + 54 hours for XBRL formatting of submission).

[437] $10,460,000 = 20 (number of SB SEF respondents) × $523,000 ($500,000 for outside accounting services for auditing SB SEF's financial statements + $23,000 in outside software and other cost for formatting financial statement submissions in XBRL format).

[438] *See* Securities Exchange Act Release No. 49616 (Apr. 26, 2004), 69 FR 24016 (Apr. 30, 2004) (outlining the Commission's calculations regarding

purposes and in order to provide an estimate that is not under-inclusive, the Commission preliminarily estimates that all respondents applying for registration as a SB SEF pursuant to proposed Rule 801, or 20 SB SEFs, may be controlled by other persons and therefore subject to the additional burden imposed on SB SEF's controlled by other persons by Exhibit P. Thus, the Commission preliminarily estimates a total additional burden for all SB SEFs that are controlled by other persons to comply with the opinion of counsel requirements of Exhibit P of 20 hours [439] and $18,000.[440] The Commission solicits comments as to the accuracy of these estimates.

Pursuant to the requirements of proposed Rule 801(f), Exhibit P to proposed Form SB SEF would require a non-resident SB SEF to provide an opinion of counsel that the SB SEF can, as a matter of law, provide the Commission with access to the books and records of the SB SEF and submit to onsite inspection and examination by representatives of the Commission. This creates an additional burden for non-resident SB SEFs. Based on similar requirements on Form 20–F, the Commission preliminarily estimates that this additional burden would add 1 hour and $900 in outside legal costs per respondent.[441] For PRA purposes, the Commission preliminarily estimates that one out of the 20 estimated persons applying for registration as a SB SEF pursuant to proposed Rule 801 may be "non-resident" SB SEFs and therefore subject to the additional burden imposed on non-resident SB SEFs by Exhibit P. Thus, the Commission preliminarily estimates a total additional burden for all non-resident SB SEFs to comply with the opinion of counsel requirements of Exhibit P of 1 hour [442] and $900.[443]

Therefore, the Commission preliminarily estimates that the total one-time burden for a SB SEF to prepare and file the initial Form SB SEF, including all exhibits thereto except for Exhibit P, would be 694 hours [444] and $523,000.[445] In addition, SB SEFs controlled by other persons and non-resident SB SEFs would incur an additional one-time burden of 1 hour and $900 to prepare and file Exhibit P to proposed Form SB SEF. This would result in a total initial burden for all SB SEFs of 13,901 hours [446] and $10,478,900.[447] The Commission requests comment on the accuracy of these estimates.

The Commission preliminarily estimates that each SB SEF would file four amendments to Form SB SEF pursuant to proposed Rules 802(a) and (b) per year, and that each SB SEF would incur an average burden of 25 hours to prepare each amendment pursuant to proposed Rules 802(a) and (b), for a total annual burden of 100 hours. The Commission bases this estimate on previous Commission estimates relating to amendments to Form 1 filed by national securities exchanges pursuant to Rule 6a–2 under the Exchange Act.[448] The Commission preliminarily believes that SB SEFs would prepare these amendments to Form SB SEF internally.

The Commission preliminarily believes that two registered SB SEFs that are controlled by other persons out of all registered SB SEFs that are controlled by other persons per year would be required to file an amendment to Exhibit P to Form SB SEF pursuant to proposed Rule 802(c) due to changes in the legal or regulatory framework of any person that controls such SB SEFs. The Commission preliminarily believes that a SB SEF controlled by another person would incur the same burden to prepare an amended Exhibit P as it would to prepare the initial Exhibit P. Therefore, the Commission preliminarily estimates that a SB SEF controlled by another person would incur an average burden of 1 hour and $900 to prepare an amended Exhibit P pursuant to proposed Rule 802(c) per year,[449] and that all SB SEFs controlled by other persons would incur an aggregate burden of 2 hours [450] and $1,800 per year [451] to prepare amended Exhibit Ps pursuant to proposed Rule 802(c).

The Commission preliminarily believes that one non-resident SB SEF would be required to file one amendment to Exhibit P to Form SB SEF pursuant to proposed Rule 802(d) per year. The Commission preliminarily believes that a non-resident SB SEF would incur the same burden to prepare an amended Exhibit P as it would to prepare the initial Exhibit P. Therefore, the Commission preliminarily estimates that a non-resident SB SEF would incur an average burden of 1 hour and $900 to prepare each amended Exhibit P pursuant to proposed Rule 802(d) per year,[452] and that this estimate represents the aggregate burden for all non-resident SB SEFs per year.

The Commission believes that each SB SEF would file one update to Form SB SEF pursuant to proposed Rule 802(f) per year, and that it would take a SB SEF a longer time to file an annual update to Form SB SEF pursuant to proposed Rule 802(f) than it would take a SB SEF to file an amendment to Form SB SEF pursuant to proposed Rules

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the PRA burdens resulting from having to provide a legal opinion and additional disclosure required by Instruction 3 to Item 7.B to Form 20–F). The Commission calculated that such requirements would result in an additional burden to affected foreign private issuers of 3 hours, of which 25%, or approximately 1 hour, would be incurred by the foreign private issuers themselves, and 75% would be incurred by outside firms, including legal counsel, which would cost approximately $900 ($900 = 3 hours (estimated burden to comply with proposed Rule 801(f)) × 0.75 (portion of estimated burden incurred by outside legal counsel × $400 (hourly rate for an outside attorney)). The Commission preliminarily continues to estimate the hourly rate for an outside attorney at $400 per hour, based on industry sources. *See* Securities Exchange Act Release No. 62184A (May 27, 2010), 75 FR 33100 at note 505 (June 10, 2010) ("Municipal Securities Disclosure Release").

[439] 20 hours = 20 (number of SB SEF respondents controlled by other persons) × 1 (hourly burden to comply with Exhibit P).

[440] $18,000 = 20 (number of SB SEF respondents controlled by other persons) × $900 (cost for outside legal services to comply with Exhibit P).

[441] *See supra* note 438.

[442] 1 hour = 1 (number of non-resident SB SEF respondents) × 1 (hourly burden to comply with Exhibit P).

[443] $900 = 1 (number of non-resident SB SEF respondents) × $900 (cost for outside legal services to comply with Exhibit P).

[444] 694 hours = 100 hours to comply with Form SB SEF except for Exhibits F, H and P + 500 hours for audited SB SEF financial statements + 40 hours for unaudited financial statements of affiliated entities + 54 hours for XBRL formatting of submission.

[445] $523,000 = $500,000 for outside accounting services for auditing SB SEF's financial statements + $23,000 in outside software and other cost for formatting financial statement submission in XBRL format.

[446] 13,901 = (20 (number of SB SEF respondents) × 694 hours (total initial burden to comply with Form SB SEF except for Exhibit P)) + (20 (number of SB SEF respondents controlled by other persons) × 1 hour (total initial burden to comply with Exhibit P)) + (1 (number of non-resident SB SEF respondents) × 1 hour (total initial burden to comply with Exhibit P).

[447] $10,478,900 = (20 (number of SB SEF respondents) × $523,000 (total initial cost to comply with Form SB SEF except for Exhibit P)) + (20 (number of SB SEF respondents controlled by other persons) × $900 (total initial cost to comply with Exhibit P)) + (1 (number of non-resident SB SEF respondents) × $900 (total initial cost to comply with Exhibit P)).

[448] The Commission calculated in 2010 that national securities exchanges file four amendments or periodic updates to Form 1 per year, incurring an average burden of 25 hours per amendment to comply with Rule 6a–2. *See* 75 FR 32824, *supra* note 430. While the requirements of Rule 6a–2 are not identical to the requirements of proposed Rules 802(a) and (b), the Commission believes that there is sufficient similarity for PRA purposes that the burden would be equivalent.

[449] *See supra* note 438 and accompanying text.

[450] 2 = 2 (number of SB SEFs controlled by other persons required to file an amended Exhibit P pursuant to proposed Rule 802(c) per year) × 1 hour (total annual burden to file an amended Exhibit P).

[451] $1,800 = 2 (number of SB SEFs controlled by other persons required to file an amended Exhibit P pursuant to proposed Rule 802(c) per year) × $900 (total annual cost burden to file an amended Exhibit P).

[452] *See supra* note 441 and accompanying text.

802(a) and (b), but less time than it would take a SB SEF to prepare an initial application on Form SB SEF. For each annual update to Form SB SEF, the SB SEF should be able to compile and submit the information more readily than it would take for the initial Form SB SEF submission because the SB SEF should already have much of the information required by the annual update in its possession. Therefore, the Commission preliminarily estimates that each SB SEF would incur an average burden of 50 hours to prepare each annual update to the Form SB SEF pursuant to proposed Rule 802(f).[453]

The Commission estimates that the annual burden for all respondents to file amendments and periodic updates to the Form SB SEF pursuant to proposed Rule 802 would be 3,003 hours[454] and $2,700.[455] The Commission requests comment on the accuracy of its estimates.

The Commission preliminarily estimates that the preparation and filing of supplemental information pursuant to proposed Rule 803(a) generally would involve photocopying existing documents and therefore should take less than one-half hour per response. The Commission similarly preliminarily estimates that where a SB SEF chooses to comply with the requirements of proposed Rule 803(b), which relates to supplemental information being made available continuously on the SB SEF's Web site, instead of proposed Rule 803(a), which relates to filing of the actual supplemental information, the response required by proposed Rule 803(b) should take less than one-half hour as well. The Commission preliminarily estimates that each SB SEF would make approximately 15 filings on an annual basis pursuant to proposed Rules 803(a) and (b) combined. The Commission bases these estimates on previous Commission estimates relating to supplemental material filed by national securities exchanges pursuant to Rule 6a–3.[456] Therefore, the Commission estimates that the total annual reporting burden under proposed Rule 803 for all SB SEFs would be 150 hours.[457] The Commission requests comment on the accuracy of this estimate.

Proposed Rule 804 would require that a SB SEF provide the Commission notice of withdrawal of registration and file an amended Form SB SEF to update any inaccurate information at the time of such notice of withdrawal. The Commission preliminarily estimates that one SB SEF per year would seek to withdraw its registration with the Commission and therefore be subject to the collection of information requirements in proposed Rule 804. The Commission preliminarily estimates that a SB SEF would incur an average burden of 1 hour to prepare and file with the Commission a notice of withdrawal of registration. The Commission preliminarily believes that the burden incurred by a SB SEF withdrawing its registration to file an amended Form SB SEF pursuant to proposed Rule 804 would be included in the estimated burden under proposed Rule 802(f) requiring annual updates to Form SB SEF. Therefore, the Commission estimates that the annual burden for all respondents pursuant to proposed Rule 804 would be 1 hour.

The Commission preliminarily estimates that the total annual hourly burden for all SB SEFs combined to comply with the registration requirements under Regulation SB SEF would be 3,154 hours[458] and the total one time hourly burden would be 13,901 hours.[459] The Commission preliminarily estimates that the total annual cost burden for all SB SEFs to comply with the registration requirements under Regulation SB SEF would be $2,700,[460] and the total one-time cost burden for all SB SEFs would be $10,478,900.[461] The Commission requests comment on the accuracy of these estimates.

2. Rule-Writing Requirements for SB SEFs

The proposed rules that would require a SB SEF to establish rules, policies and procedures to meet the requirements of various proposed rules in Regulation SB SEF are summarized in Section XXII.A.2. above. Based on its experience with the rule-writing process conducted by national securities exchanges and applicants to become national securities exchanges, the Commission believes that a SB SEF would spend an average of 10 hours to draft each rule, policy or procedure required to be established under Regulation SB SEF and that the SB SEF would handle this work internally. The Commission recognizes that in some cases, the SB SEF may take longer than 10 hours to draft a particular rule, policy or procedure, but in other cases, the SB SEF may take fewer than 10 hours to draft a particular rule, policy or procedure. Therefore, the Commission preliminarily believes that the 22 proposed rules, policies and procedures that a SB SEF would be required to draft under proposed Regulation SB SEF would carry a one-time paperwork burden of 220 hours per respondent, for a maximum total of 4,400 hours.[462] The estimated 220 hours per respondent also would include the time expended for review of the draft rules, policies or procedures by the SB SEF's management. The Commission requests

[453] Proposed Rules 811(b)(4) and 811(g)(2) would require SB SEFs to report information regarding grants, denials and limitations of access on Form SB SEF and to disclose all disciplinary actions taken annually on an amendment to Form SB SEF, respectively. In addition, proposed Rule 804(a) would require that a SB SEF intending to file a notice of withdrawal from registration as a SB SEF with the Commission file an amended Form SB SEF to update any inaccurate information at the time of such notice of withdrawal. The Commission preliminarily believes that the burdens associated with these requirements would be included in the burden associated with the annual update to Form SB SEF required by proposed Rule 802(f).

The Commission notes that, pursuant to proposed Rules 823(e)(1) and (2), the CCO of a SB SEF would be required to prepare annual updates to the financial reports required by Exhibits F and H. Therefore, the Commission preliminarily believes that any burden resulting from the requirement to update Exhibits F and H annually pursuant to proposed Rule 802(f) would be included in the burden associated with proposed Rule 823(e)(1) and (2) discussed in the sections of this PRA analysis relating to the duties of the SB SEF's CCO.

[454] 3,003 hours = (20 (number of SB SEF respondents) × 4 (number of filings pursuant to proposed Rules 802(a) and (b)) × 25 hours (burden per filing)) + (2 (number of respondents) × 1 (number of filings pursuant to proposed Rule 802(c)) × 1 hour (burden per filing)) + (1 (number of respondents) × (1 (number of filings pursuant to proposed Rule 802(d)) × 1 hour (burden per filing)) + (20 (number of SB SEF respondents) × (1 (number of filings pursuant to proposed Rule 802(f)) × 50 hours (burden per filing)).

[455] $2,700 = (2 (number of respondents) × 1 (number of filings pursuant to proposed Rule 802(c)) × $900 (burden per filing)) + (1 (number of respondents) × 1 (number of filings pursuant to proposed Rule 802(d)) × $900 (burden per filing)).

[456] The Commission calculated in 2010 that Rule 6a–3 would require national securities exchanges to make 25 filings per year at a burden of 0.5 hours per filing. 75 FR 32822 (June 9, 2010) (outlining the most recent Commission calculations regarding the PRA burdens for Rule 6a–3). While the requirements of Rule 6a–3 are not identical to those of proposed Rule 803, the Commission believes that there is sufficient similarity for PRA purposes that the burden would be equivalent. However, Rule 6a–3 contains a requirement for national securities exchanges to file certain monthly reports, while proposed Rule 803 contains no such requirement with respect to SB SEFs. Therefore, the Commission preliminarily estimates that a SB SEF would make 15 filings per year pursuant to proposed Rule 803, rather than 25 filings as estimated in connection with Rule 6a–3.

[457] 150 hours = 20 (number of SB SEF respondents) × 15 (number of filings per respondent) × .5 hours (burden per filing).

[458] 3,154 hours = 3,003 (estimated hourly burden to comply with proposed Rule 802) + 150 (estimated hourly burden to comply with proposed Rule 803) + 1 (estimated hourly burden to comply with proposed Rule 804).

[459] *See supra* note 446.

[460] *See supra* note 455.

[461] *See supra* note 447.

[462] 4,400 hours = 20 (number of SB SEF respondents) × 220 hours (one-time burden to draft 22 proposed rules, policies and procedures).

comment on the accuracy of this estimate.

The Commission preliminarily estimates that once a SB SEF has drafted the written rules, policies and procedures that it is required to establish pursuant to Regulation SB SEF, a SB SEF would spend approximately 10 hours per month to review its written rules, policies and procedures to ensure that they are up-to-date and remain in compliance with proposed Regulation SB SEF and to prepare any necessary new or amended rules, policies and procedures.[463] Therefore, the Commission preliminarily estimates that the provisions of proposed Regulation SB SEF requiring that a SB SEF establish certain rules, policies and procedures would result in an ongoing annual burden of 120 hours per respondent,[464] for a total estimated ongoing annual burden of 2,400 hours.[465] The Commission requests comment on the accuracy of this estimate.

3. Reporting Requirements for SB SEFs

Proposed Rule 814: Proposed Rule 814(a) would require a SB SEF to require its participants to provide information or documents to the SB SEF upon request. Proposed Rule 814(a) also would require the SB SEF to require its participants to provide information or documents to any representative of the Commission upon request.

As noted above, the Commission estimates that each SB SEF would have 275 participants.[466] Based on industry sources, the Commission believes it is likely that each participant would elect to be a member of each SB SEF. The Commission therefore estimates that each of these estimated 275 participants would be a participant of each SB SEF. The Commission therefore estimates that there would be a total of 275 SB SEF participants subject to the collection of information requirements of proposed Rule 814(a). The Commission requests comment on the accuracy of this estimate.

Based on its experience in requesting information from exchanges and exchange members for various purposes, the Commission estimates that it would require an average of 25 hours per response for a SB SEF participant to compile and transmit documents and information requested pursuant to proposed Rule 814(a) and that such requests would occur a total of 4 times each year per SB SEF participant.[467] Thus, the Commission estimates that the annual burden on each SB SEF participant to report documents or information pursuant to proposed Rule 814(a) would be 100 hours.[468] The Commission therefore estimates that the annual aggregate burden on SB SEF participants for all SB SEFs would be 27,500 hours.[469] The Commission believes that this work, should it be required, would be conducted internally. The Commission seeks comment on these proposed estimates.

Proposed Rule 814(b)(2) would require a SB SEF to provide information or documents to any representative of the Commission upon request. For PRA purposes, the Commission estimates that it would request information or documents under proposed Rule 814(b)(2) two times per year, per respondent. The amount of time that it would take for a respondent to comply with a request would vary depending on the nature and extent of the request. Based on its experience in requesting information from exchanges for a variety of purposes, the Commission estimates that it would require an average of 25 hours per response for a SB SEF to compile and transmit documents and information requested by the Commission, for an annual hourly burden of 50 hours per respondent. Thus, the Commission preliminarily estimates the aggregate annual burden on a SB SEF to comply with requests for documents or information pursuant to proposed Rule 814(b)(2) would be 1,000 hours.[470] The Commission believes that this work, should it be required, would be conducted internally. The Commission solicits comment as to the accuracy of these estimates.

Proposed Rule 814(b)(3) would require a SB SEF to have the capacity to carry out such international information-sharing agreements as the Commission may require. If so directed by the Commission, a SB SEF could be required to carry out one or more international-information sharing agreements. It is difficult to estimate how many international information-sharing agreements the Commission may direct a SB SEF to carry out or what the reporting requirements under such agreements may be.

The Commission estimates, for PRA purposes only, that SB SEFs would need to carry out such an agreement, on average, once per year. The Commission further estimates that each such agreement could require 40 hours per respondent to prepare, review and finalize. The Commission therefore preliminarily estimates that the paperwork burden for SB SEFs associated with having the capacity to carry out international information-sharing agreements as the Commission may require pursuant to proposed Rule 814(b)(3) would be 800 hours.[471] The Commission believes that these agreements initially would be created or reviewed internally, but also reviewed by outside counsel. The Commission estimates that the SB SEF's outside counsel would require 10 hours to review these documents for a cost of $4,000 per respondent, and a total cost of $80,000 for all respondents.[472] The Commission solicits comment as to the accuracy of these estimates.

In addition, the Commission preliminarily estimates that a SB SEF would be required to provide information pursuant to an international information-sharing agreement a total of twice per year and that, similar to complying with a Commission request for information pursuant to other provisions of proposed Rule 814, it would require 25 hours per response to comply with a request for information, for a total annual burden of 50 hours per year per SB SEF. The Commission believes that this work, should it be required, would be conducted internally. The Commission therefore estimates that aggregate annual paperwork burden on SB SEFs associated with reporting under international information-sharing agreements entered into under proposed

[463] This burden estimate does not include the burden that would be incurred by a SB SEF in connection with submitting rule filings in connection with new rules or rule amendments to the Commission, which burden would be included in the burden for proposed Rules 805 and 806 discussed in the sections of this PRA relating to the rule filing processes for SB SEFs.

[464] 120 hours = 10 hours (monthly burden) × 12 (months per year).

[465] 2,400 hours = 20 (number of SB SEF respondents) × 120 hours (annual burden to update rules, policies and procedures required by proposed Regulation SB SEF).

[466] *See supra* note 429.

[467] The estimate of 4 annual requests assumes that each SB SEF participant would receive, on average, one request for information per calendar quarter.

[468] 100 hours = 4 (number of requests annually) × 25 (annual hourly burden for each participant to comply with SB SEF rules imposed pursuant to proposed Rule 814(a)).

[469] 27,500 hours = 4 (total number of annual requests made of a SB SEF participant directly or indirectly) × 25 (hours per respondent) × 275 (number of SB SEF participants required to comply with proposed rules imposed by a SB SEF pursuant to proposed Rule 814(a)).

[470] 1,000 hours = 50 (annual hourly burden to comply with proposed Rule 814(b)(2)) × 20 (number of SB SEF respondents).

[471] 800 hours = 40 (annual hourly burden to enter into an international information-sharing agreement pursuant to proposed Rule 814(b)(3) × 20 (number of SB SEF respondents). The Commission believes there would be no separate initial burden.

[472] These figures are based on an hourly cost of outside counsel at $400. *See* Municipal Securities Disclosure Release, *supra* note 438.

Rule 814(b)(3) would be 1,000 hours.[473] The Commission solicits comment as to the accuracy of these estimates.

The Commission therefore estimates the aggregate annual paperwork burden associated with proposed Rule 814 to be 27,500 hours for SB SEF participant respondents and 2,800[474] hours and $80,000 for SB SEF respondents.

Proposed Rule 816: Proposed Rule 816 would require a SB SEF to notify the Commission of any exercise of its emergency authority, and within two weeks following cessation of an emergency, submit to the Commission a report explaining the basis for declaring an emergency, how conflicts of interest were minimized, and the extent to which the SB SEF considered the effect of its emergency action on the markets for the SB swap and any security or securities underlying the SB swap. The collection of information associated with proposed Rule 816 would apply only during and following an emergency.[475]

The Commission notes that emergencies in the securities markets are rare, but when they do occur, they require significant time and resources to address. For PRA purposes only, the Commission estimates that a SB SEF would exercise its emergency authority once per year. Based on its experience with national securities exchanges, the Commission estimates that the time that would be necessary for a SB SEF to prepare and transmit the notice and report regarding emergency authority pursuant to proposed Rule 816 would be 40 hours per respondent. Thus, the Commission estimates that the total annual reporting burden associated with proposed Rule 816 would be 800 hours.[476] The Commission believes that this work, should it be required, would be conducted internally. The Commission solicits comment on these estimates.

Proposed Rule 818: Proposed Rule 818(e) would require a SB SEF to report to the Commission such information as the Commission may, from time to time, determine to be necessary to perform the duties of the Commission. For PRA purposes only, the Commission estimates that the Commission may request such information from a SB SEF once each year. For PRA purposes only, the Commission estimates that any request for information would be information easily accessible to the SB SEF, but could require an analysis of such information by the SB SEF. Based on the Commission's experience with information requested of other registered entities, the Commission preliminarily estimates that each request pursuant to proposed Rule 818 would require 20 hours to collect, review, draft any accompanying analysis or report, and transmit, which would result in an annual hourly burden of 20 hours per SB SEF respondent. Thus, the Commission estimates that the aggregate annual reporting burden on SB SEFs associated with proposed Rule 818(e) would be 400 hours.[477] The Commission solicits comment on these estimates.

Proposed Rule 818(f) would require a SB SEF to provide to any representative of the Commission, upon request, copies of documents required to be kept and preserved pursuant to the recordkeeping requirements of proposed Rule 818. For PRA purposes only, the Commission preliminarily estimates that it would request information or documents under proposed Rule 818(f) twice per year and would require no more than 25 hours per response to compile and transmit, resulting in an annual hourly burden of 50 hours per SB SEF respondent.[478] The Commission therefore estimates the annual aggregate paperwork burden associated with proposed Rule 818(f) would be 1,000 hours.[479] The Commission solicits comment on these estimates.

The Commission therefore estimates the total annual reporting burden on SB SEFs associated with proposed Rule 818 would be 1,400 hours.[480]

Proposed Rule 822: Proposed Rule 822(a)(2) would require a SB SEF to submit to the Commission an annual objective review of the capability of SB SEF systems that support or are integrally related to the performance of the SB SEF's activities. If the objective review is performed by an internal department, an objective, external firm would be required to assess the internal department's objectivity, competency, and work performance. Based on its experience with its ARP program, the Commission believes that the annual burden per respondent of conducting an internal audit would be approximately 625 hours.[481] Further, the Commission's experience with the ARP program has indicated that an additional 200 hours per respondent per year would be required on average to oversee and establish the independent review of these audits.[482] Thus, the Commission estimates the aggregate annual burden on SB SEFs to comply with requirement to submit these reports would be 16,500 hours.[483] In addition, based on its experience with the ARP program,[484] the Commission estimates that the annual cost to hire an objective, external firm to be approximately $90,000 per respondent annually. For this reason, the Commission estimates the total annual cost of hiring an objective, external firm to review internal audits as $1,800,000 for all respondents.[485] The Commission solicits comment as to the accuracy of this information.

In addition, proposed Rule 822(a)(3) would require a SB SEF to promptly notify the Commission in writing of material systems outages and submit to the Commission within five business days of when the outage occurred a written description and analysis of the outage and any remedial measures that have been implemented or are

[473] 1,000 hours = 50 (annual hourly burden to comply with reporting requirements pursuant to international information-sharing agreements × 20 (number of SB SEF respondents).

[474] 2,800 hours = 1,000 (aggregate burden on SB SEF respondents to comply with proposed Rule 814(b)(2)) + 1,800 hours (aggregate burden on SB SEF respondent to comply with proposed Rule 814(b)(3)).

[475] Proposed Rule 816(d)(2) provides that if a SB SEF implements any rule or rule amendment in the exercise of its emergency authority, it must file such rule or rule amendment with the Commission pursuant to proposed Rule 806 prior to the implementation of such rule or rule amendment, or, if not practicable, within 24 hours after implementation of such rule or rule amendment. The annual hourly burden to comply with proposed Rule 816(d)(2) is included in the estimated annual hourly burden for a SB SEF to comply with proposed Rule 806.

[476] 800 hours = 40 (annual hourly burden to comply with proposed Rule 816) × 20 (number of SB SEF respondents).

[477] 400 hours = 20 (annual hourly burden to comply with proposed Rule 818(e)) × 20 (number of SB SEF respondents). The Commission believes there would be no separate initial burden.

[478] Based on its experience in requesting information from exchanges for a variety of purposes, the Commission estimates that it would require an average of 25 hours per response for a SB SEF to compile and transmit documents and information requested by the Commission.

[479] 1,000 hours = 25 (annual hourly burden to comply with proposed Rule 818(f)) × 20 (number of SB SEF respondents).

[480] 1,400 hours = 400 (hourly burden to comply with proposed Rule 818(e)) + 1,000 (hourly burden to comply with proposed Rule 818(f)).

[481] *See* SDR Release, *supra* note 6.

[482] *Id.*

[483] 16,500 hours = 825 (annual hourly burden to comply proposed Rule 822(a)(2)) × 20 (number of SB SEF respondents).

[484] Under the Commission's ARP inspection program of SROs and certain ATSs, the Commission staff conducts on-site inspections and attends periodic technology briefings presented by SRO and ATS staff for the Commission's ARP staff, which generally covers systems capacity and testing, review of system vulnerability, review of planned system development, and business continuity planning. Under the ARP inspection program, the Commission staff also monitors system failures and planned system changes on a daily basis.

[485] $1,800,000 = $90,000 (annual external dollar cost per respondent to comply with proposed Rule 822(a)(2)) × 20 (number of SB SEF respondents).

contemplated. The Commission estimates, based on its experience with the ARP program, that the burden imposed by these requirements would be 15.4 hours on average per respondent per year, for a total estimated burden of 308 hours per year for all respondents.[486] The Commission believes that this work would be conducted internally. The Commission solicits comments as to the accuracy of this estimate.

Proposed Rule 822(a)(4) would require a SB SEF to notify the Commission in writing at least thirty calendar days before implementation of any planned material systems changes. The Commission estimates that there would be an average of 60 such events per respondent per year.[487] Based on the Commission's experience with the ARP program, the Commission estimates that each of these notices would require an average of 2 hours for a total burden for all respondents of 2,400 hours annually.[488] The Commission believes that this work would be conducted internally. The Commission solicits comments as to the accuracy of this estimate.

The Commission therefore preliminarily estimates that the total annual hourly reporting burden associated with proposed Rule 822 would be 19,208 hours [489] and $1,800,000.[490]

The Commission preliminarily estimates that the total annual hourly burden for all SB SEFs combined for reporting would be 24,208 hours.[491] There is no one time initial hourly burden associated with the proposed reporting requirements. The Commission preliminarily estimates that the total annual cost burden for all SB SEFs combined for reporting would be $1,880,000.[492] In addition, the Commission preliminarily estimates that the total annual hourly burden on all SB SEF participants for reporting under proposed Regulation SB SEF would be 28,000 hours.

4. Recordkeeping Required Under Regulation SB SEF

The annual recordkeeping requirements that are contained in proposed Rules 818(a) and (b) are similar to the requirements that apply to SROs pursuant to Rules 17a–1(a) and (b) under the Exchange Act.[493] The Commission currently estimates that an SRO, including a national securities exchange, would expend approximately 50 hours per year to comply with the collection of information requirement of Rule 17a–1.[494] Based on the Commission's experience with Rule 17a–1(a) and (b), the Commission believes that 50 hours would be an appropriate estimate for the hourly burden that would apply to SB SEFs to comply with proposed Rule 818(a) and (b). The Commission notes that SB SEFs generally would be electronic platforms and that the vast preponderance of its records thus should be retained electronically in the ordinary course of its business. Therefore, the Commission preliminarily estimates that it would take a SB SEF approximately 50 hours annually to comply with proposed Rule 818(a) and (b) for an aggregate annual burden of 1,000 hours.[495] This estimated amount includes, but is not limited to, the annual hourly burden to generate, collect, organize and preserve all of the documents and other records required under proposed Rule 818(a) and (b). The Commission requests comment on the accuracy of this estimate.

In addition, proposed Rule 818(c) would require a SB SEF to keep certain records with respect to trading activity on and through the SB SEF. Specifically, a SB SEF would be required to make and keep accurate, time-sequenced records of all trading interest and transactions that are received by, originated on, or executed on the SB SEF. This recordkeeping rule is similar to the audit trail requirement that applies to ATSs pursuant to Rule 302 of Regulation ATS under the Exchange Act.[496] The Commission currently estimates that an ATS would expend approximately 130 hours per year to comply with the collection of information requirements of Rule 302 of Regulation ATS. Based on the Commission's experience with Rule 302 of Regulation ATS, which contains the requirement that an ATS make and keep records necessary to create a meaningful audit trail, the Commission preliminarily estimates that the annual hourly paperwork burden for a SB SEF to comply with proposed Rule 818(c) would be approximately 130 hours, which would result in an aggregate annual burden of 2,600 hours.[497] The Commission requests comment on the accuracy of this estimate.

The Commission preliminarily believes that the records that a SB SEF would have to keep and preserve to comply with proposed Rule 818 would be the same records that a SB SEF would already have to keep and preserve in the ordinary course of its business. A SB SEF would be required to keep and preserve these records to, among other things, pay taxes, defend against legal actions, resolve conflicts between participants, and generally to ensure the smooth functioning of the SB SEF's business operations. Therefore, the Commission preliminarily believes that, while there would be a collection of information required by proposed

[486] 308 hours = 15.4 annual hourly burden per respondent to comply proposed Rule 822(a)(3)) × 20 (number of SB SEF respondents). This annual hourly burden comports with the Commission's estimate for similar proposed requirements to be imposed on SDRs to comply with similar proposed requirements. *See* SDR Release, *supra* note 6.

[487] This estimate would account for any weekly maintenance that would meet the standard of a "material systems change," as well as for any software upgrades, throughout the year, that would meet such standard.

[488] 2,400 hours = 60 (notices per SB SEF) × 2 (annual hourly burden per notice) × 20 (number of SB SEF respondents). *See* SDR Release, *supra* note 6.

[489] 19,208 hours = 16,500 (annual hourly burden to comply with proposed Rule 822(a)(2)) + 308 (annual hourly burden to comply with proposed Rule 822(a)(3)) + 2,400 (annual hourly burden to comply with proposed Rule 822(a)(4)).

[490] *See supra* note 485.

[491] 24,208 = 2,800 (annual hourly burden to comply with proposed Rule 814) + 800 (annual hourly burden to comply with proposed Rule 816) + 1,400 (annual hourly burden to comply with proposed Rule 818) + 19,208 (annual hourly burden to comply with proposed Rule 822).

[492] $1,880,000 = $80,000 (annual cost burden to comply with proposed Rule 814(b)(3)) + $1,800,000 (annual cost burden to comply with proposed Rule 822(a)(2)).

[493] 17 CFR 240.17a–1(a) and (b). In addition, proposed Rule 811(b)(3) would require that a SB SEF make and keep records relating to all grants and denials of access to the SB SEF and proposed Rule 811(g) would require a SB SEF to make and keep records relating to all disciplinary proceedings. The records required by proposed Rules 811(b)(3) and 811(g) would be included in the business records required to be kept pursuant to proposed Rule 818. Therefore, the Commission preliminarily believes that the paperwork burden for these rules would be included in the estimated burden for proposed Rule 818. *See supra* note 417 and accompanying text.

[494] Rule 17a–1 also states generally that SROs shall, upon the request of any representative of the Commission, promptly furnish copies of documents required to be kept and preserved under the rule. *See* 17 CFR. 240.17a–1. The Commission's estimated burden of 50 hours per respondent reflects compliance with all of the recordkeeping provisions of this rule. *See* 2010 Extension of Rule 17a–1 Supporting Statement, Office of Management and Budget, available at *http://www.reginfo.gov/public/do/PRAViewDocument?ref_nbr=201007-3235-003.*

[495] 1,000 hours = 20 (number of SB SEF respondents) x 50 hours (annual hourly burden to comply with proposed Rule 818(a) and (b)).

[496] Rule 302 of Regulation ATS under the Exchange Act generally requires an ATS to keep a record of subscribers, daily summaries of trading and time sequenced records of order information in the ATS. *See* 17 CFR 242.302. The Commission's estimated burden of 130 hours per respondent reflects compliance with all of the recordkeeping provisions of this rule. *See* 2010 Extension of Rule 302 Supporting Statement, Office of Management and Budget, available at *http://www.reginfo.gov/public/do/PRAViewDocument?ref_nbr=201006-3235-008.*

[497] 2,600 hours = 20 (number of SB SEF respondents) x 130 hours (annual hourly burden to comply with proposed Rule 818(c)).

Rule 818 related to recordkeeping, there would not be a paperwork burden for PRA purposes associated with the SB SEF's complying with proposed Rule 818 aside from establishing or modifying recordkeeping systems as noted below, because these records would be maintained in the ordinary course of its business.[498]

For purposes of the PRA, however, the Commission preliminarily estimates that a SB SEF could incur a one-time burden to set up or modify an existing recordkeeping system to comply with the proposed Rule 818. Based on the Commission's experience with recordkeeping costs and consistent with prior burden estimates for similar recordkeeping provisions,[499] the Commission estimates that setting up or modifying a recordkeeping system would create an initial burden of 345 hours [500] and $1,800 in information technology costs per respondent to purchase recordkeeping software,[501] for a total initial burden of 6,900 hours [502] and $36,000.[503] The Commission requests comment on the accuracy of this estimate.

Additionally, the Commission preliminarily estimates that each SB SEF may have a one-time burden to upgrade its existing systems to ensure that the audit trail component of their systems complies with proposed Rule 818(c). Based on industry sources, the Commission preliminarily believes that this work would be done internally by two programmers over the course of approximately four weeks. Therefore, the Commission preliminarily estimates that it would take a total of 320 hours for a SB SEF to upgrade its existing systems for an aggregate one-time hourly burden of 6,400 hours.[504]

Therefore, the Commission preliminarily believes that the total aggregate annual hourly burden for 20 SB SEFs to comply with proposed Rule 818(a) through (c) would be approximately 3,600 hours.[505] The total one time hourly burden for 20 SB SEFs to comply with proposed Rule 818 would be approximately 13,300 hours [506] and $36,000. The Commission requests comment on the accuracy of this estimate.

As discussed above, proposed Rule 813(c)(1) would require a SB SEF to establish rules requiring any participant that enters any trading interest or executes any transaction on the SB SEF to maintain books and records of any such trading interest or transaction and of any position in any security-based swap that is the result of any such trading interest or transaction. The Commission preliminarily believes that proposed Rule 813(c)(1) could impose a collection of information burden on some SB SEF participants.[507] However, the Commission also preliminarily believes that the records that many SB SEF participants would have to maintain pursuant to proposed Rule 813(c)(1) would be the same records that these participants would have to maintain under other Commission recordkeeping provisions to the extent they are regulated entities or in the ordinary course of their business.[508] Therefore, the Commission preliminarily believes that the paperwork burden for a number of SB SEF participants is either already encompassed in the collection of information for other recordkeeping obligations that they must comply with or would not be required to be calculated for purposes of this PRA analysis because such burden relates to the maintenance of records that are usually or customarily maintained.[509]

However, the Commission believes that proposed Rule 813(c)(1) could impose a new obligation to maintain books and records on those ECPs that would become participants of the SB SEF. For PRA purposes the Commission believes that it is appropriate to estimate that all 210 ECPs would be subject to the collection of information requirement of proposed Rule 813(c)(1).[510] Based on the Commission's experience with similar recordkeeping rules,[511] the Commission preliminarily estimates that it would take each ECP that is a SB SEF participant approximately 40 hours on an annual basis to comply with the collection of information requirement of proposed Rule 813(c)(1) for a total annual burden for all ECP respondents combined of 8,400 hours.[512] The Commission requests comment on the accuracy of this estimate.

For purposes of the PRA, the Commission also preliminarily estimates that ECPs that would be SB SEF participants could incur a one-time burden to set up or modify an existing recordkeeping system to comply with the proposed Rule 813(c)(1). Based on the Commission's experience with recordkeeping costs and consistent with prior burden estimates for similar recordkeeping provisions,[513] the Commission estimates that setting up or modifying a recordkeeping system would create an initial burden of 345 hours [514] and $1,800 in information technology costs per ECP to purchase

[498] *See* 5 CFR 1320.3(b)(2). This section generally provides that the time, effort, and financial resources necessary to comply with a collection of information that would be incurred by persons in the normal course of their activities (*e.g.,* in compiling and maintaining business records) are excluded from the definition of "burden" in the PRA if they are usual and customary.

[499] *See* Securities Exchange Act Release No. 59342 (February 2, 2009); 74 FR 6456 (February 9, 2009) (Amendments to Rules for Nationally Recognized Statistical Rating Organizations) ("NRSRO Adopting Release").

[500] *See* NRSRO Adopting Release, *supra* note 499, 74 FR at 6472, n. 154 (estimated average one-time hourly burden of 345 hours for each nationally recognized statistical ratings organization ("NRSRO") to implement a recordkeeping system to comply with Rule 17g–2 under the Exchange Act, 17 CFR 240.17g–2).

[501] *See* NRSRO Adopting Release, *id.,* 74 FR at 6472 (estimated average cost of $1,800 for each NRSRO to purchase recordkeeping software).

[502] 6,900 hours = 345 hours (estimated hourly burden for each SB SEF to implement a recordkeeping system) × 20 (number of SB SEF respondents).

[503] $36,000 = $1,800 (estimated cost to purchase recordkeeping software) × 20 (number of SB SEF respondents).

[504] 6,400 hours = 320 hours (estimated one-time hourly burden for two senior programmers working 40 hours per week for four weeks at each SB SEF to upgrade systems to comply with proposed Rule 818(c)) × 20 (number of SB SEF respondents).

[505] 3,600 hours = 1,000 hours (estimated annual hourly burden to comply with proposed Rule 818(a) and (b)) + 2,600 hours (estimated annual hourly burden to comply with proposed Rule 818(c)).

[506] 13,300 hours = 6,900 hours (total estimated one-time hourly burden for all SB SEF respondents combined to set-up or modify recordkeeping software to comply with proposed Rule 818) + 6,400 hours (total estimated one-time hourly burden for all SB SEF respondents combined to modify existing systems to comply with audit trail requirements of proposed Rule 818(c)).

[507] The Commission also notes that proposed 809(c)(2)(i) would require non-registered ECPs to meet the recordkeeping and reporting requirements established by the SB SEF pursuant to proposed Rule 813. The collection of information associated with 809(c)(2)(i) is encompassed in the burden estimates for the collection of information associated with proposed Rule 813.

[508] Section 764 of the Dodd-Frank Act requires the Commission to adopt rules governing reporting and recordkeeping for SB swap dealers and major SB swap participants. *See* Public Law 111–203, § 764. The Commission is proposing reporting and recordkeeping rules for SB swap dealers and major SB swap participants as part of a separate Commission rulemaking. *See also, e.g.,* Rules 17a–3 (records to be made by certain exchange members, brokers and dealers) and 17a–4 (records to be preserved by certain exchange members, brokers and dealers) under the Exchange Act, 17 CFR 240.17a–3 and 17 CFR 240.17a–4.

[509] *See* 5 CFR 1320.3(b)(2).

[510] *See supra* note 429 and accompanying text.

[511] *See, e.g.,* 17 CFR 240.17a–3 and 17 CFR 240.17a–4.

[512] 8,400 hours = 210 (estimated number of ECPs that could be subject to the collection of information under proposed Rule 813(c)(1)) × 40 hours (estimated annual burden for each ECPs to comply with the collection of information under proposed Rule 813(c)(1)).

[513] *See* NRSRO Adopting Release *supra* note 499.

[514] *See* NRSRO Adopting Release, *supra* note 499, 74 FR at 6472, n. 154 (estimated average one-time hourly burden of 345 hours for each NRSRO to implement a recordkeeping system to comply with Rule 17g–2 under the Exchange Act).

recordkeeping software,[515] for a total initial burden of 72,450 hours [516] and $378,000 for all ECPs combined.[517] The Commission requests comment on the accuracy of this estimate.

5. Timely Publication of Trading Information Requirement for SB SEFs

Proposed Rule 817(a) would require a SB SEF to: (1) have the capacity to electronically capture, transmit, and disseminate information on price, trading volume, and other trading data on all SB swaps executed on or through the SB SEF; and (2) make public timely information on price, trading volume, and other trading data on SB swaps to the extent required by the Commission. The Commission notes that proposed Rule 817(a)(1) would incorporate Section 3D(d)(8) of the Exchange Act but would not otherwise require a SB SEF to report SB swap transactions to a registered SDR or make public timely information on price, trading volume, and other trading data on SB swaps. Rather, the Commission has proposed that other parties be responsible for reporting of SB swap transactions to a registered SDR and for the public dissemination of certain SB swap transaction information.[518]

However, because proposed Rule 817(a) would require a SB SEF to have the capacity to electronically capture, transmit, and disseminate information on price, trading volume, and other trading data on all SB swaps executed on or through the SB SEF so that it could make such information public if required, the Commission preliminarily believes that each SB SEF could have a one-time hourly burden to modify its systems so that they have this functionality.[519] The Commission believes that for a SB SEF to ensure it has the capacity to electronically capture, transmit, and disseminate information on price, trading volume, and other trading data on all SB swaps executed on or through the SB SEF, as required by Section 3D(d)(8) and as proposed to be incorporated in proposed Rule 817(a), a SB SEF would need two computer programmers, each working four weeks. This would result in a one-time hourly burden of 320 hours [520] per SB SEF respondent, for a total annual burden on all SB SEFs of 6,400 hours.[521] The Commission solicits comment on the accuracy of these estimates.

6. Rule Filing and Product Filing Processes for SB SEFs

Under proposed Rules 805 and 806, a SB SEF would be required to submit rule filings for new rules or rule amendments, including changes to a product's terms or conditions. As noted above, the Commission estimates a total of 20 SB SEF respondents for this requirement. The proposed rules are modeled on the rule filing and product filing processes proposed by the CFTC.[522] Based on the Commission staff's consultation with CFTC staff,[523] the Commission estimates that on average these requirements would require 2.5 hours of work per rule filing, with an estimated average of 60 responses per year per respondent. This would result in a total estimated burden of 150 hours per respondent [524] and 3,000 hours for all the respondents annually.[525] Based on the Commission staff's consultation with CFTC staff, the Commission believes that the SB SEF would handle the rule filing process internally. The Commission solicits comments regarding the accuracy of its estimates.

Under proposed Rules 807 and 808, a SB SEF would be required to submit filings for new products that it makes available for trading. As outlined above, the Commission estimates a total of 20 SB SEF respondents for this requirement. Based on the Commission staff's consultation with CFTC staff,[526] the Commission estimates that on average these requirements would require 2.5 hours of work per product filing, with an estimated average of 34 responses per year per respondent. The Commission estimates that this would result in a total burden of 85 hours per respondent [527] and 1,700 hours for all the respondents annually.[528] Based on the Commission staff's consultation with the CFTC staff, the Commission believes that the SB SEF would handle product filings internally. The Commission solicits comments regarding the accuracy of its estimates.

The Commission preliminarily estimates that the total annual hourly burden for all SB SEFs to prepare and submit rule filings under proposed Rules 805 and 806 would be 3,000 hours. The Commission preliminarily estimates that the total annual hourly burden for all SB SEFs to prepare and submit product filings under proposed Rules 807 and 808 would be 1,700 hours.

7. Requirements Relating to the SB SEF's CCO

The SB SEF's CCO would have several initial and annual paperwork burdens under proposed Rule 823(b)(6) and (7) and also under proposed Rule 823(c) through (e).

Under proposed Rule 823(b)(6) and (7), the CCO would be responsible for: (1) Establishing procedures for the remediation of noncompliance issues identified by the CCO identified through any compliance office review, look-back, internal or external audit finding, self-reported error or validated complaint, and (2) establishing appropriate procedures for the handling, management response, remediation, retesting, and closing of noncompliance issues. As noted above, the Commission estimates a total of 20 respondents for this requirement. Based on the Commission's paperwork burden estimates for compliance program rules adopted under the Investment Company Act of 1940 ("ICA") and the Investment Advisers Act of 1940,[529] the

[515] *See* NRSRO Adopting Release, *supra* note 499, 74 FR at 6472 (estimated average cost of $1,800 for each NRSRO to purchase recordkeeping software).

[516] 72,450 hours = 345 hours (estimated hourly burden for each SB SEF participant to implement a recordkeeping system) × 210 (estimated number of ECP SB SEF participants that could seek to set up or modify a recordkeeping system to comply with proposed Rule 813(c)(1)).

[517] $378,000 = $1,800 (estimated cost to purchase recordkeeping software) × 210 (estimated number of ECP SB SEFs that could seek to purchase recordkeeping software to comply with proposed Rule 813(c)(1)).

[518] *See* Reporting and Dissemination Release *supra* note 6.

[519] The Commission believes that a SB SEF would seek to ensure that it has the capacity to electronically capture, transmit, and disseminate information on price, trading volume, and other trading data on all SB swaps executed on or through its facilities in the ordinary course of its business. Therefore the Commission is not including the one-time burden of developing and implementing systems having the capacity to electronically capture, transmit, and disseminate information on price, trading volume, and other trading data on all SB swaps executed on or through the SB SEF in its paperwork burden estimate for proposed Rule 817(a). *See* 5 CFR 1320.3(b)(2).

[520] 320 hours = 2 (number of senior programmers) × 40 (hours in a standard full-time work week) × 4 (number of weeks required).

[521] 6,400 hours = 320 (estimated one-time hourly burden per SB SEF respondent pursuant to proposed Rule 817(a)) × 20 (number of SB SEF respondents).

[522] *See* 75 FR 67282 (November 2, 2010) (CFTC proposal to amend 17 CFR 40.2–40.5).

[523] *See id.*

[524] 150 hours = 60 (number of responses per year per respondent) × 2.5 hours (burden per response).

[525] 3,000 hours = 150 hours (annual burden per respondent pursuant to proposed Rules 805 and 806) × 20 (number of respondents).

[526] *See* 75 FR 67282 (November 2, 2010) (CFTC proposal to amend 17 CFR 40.2–40.5).

[527] 85 hours = 34 (number of responses per year per respondent) × 2.5 hours (burden per response).

[528] 1,700 hours = 85 hours (annual burden per respondent pursuant to proposed Rules 807 and 808) × 20 (number of SB SEF respondents).

[529] Rule 38a–1 under the ICA (17 CFR 270.38a–1) requires each registered investment company and business development company to adopt and implement policies and procedures reasonably designed to prevent violations of the Federal securities laws. *See* Investment Company Act

Continued

Commission estimates that, on average, the requirements of proposed Rule 823(b)(6) and (7) would mean that each SB SEF would expend 160 hours initially [530] to create the required two policies and procedures, for a total estimated burden for all respondents of 3,200 hours initially.[531] Also, due to the novel nature of the CCO requirements in the SB SEF industry and the new requirements under the Dodd-Frank Act, the Commission estimates that an initial one-time burden of $40,000 in outside legal costs [532] would be incurred per respondent, for a total outside cost burden for all respondents of $800,000.[533] The Commission solicits comments regarding the accuracy of these estimates.

A CCO also would be required under proposed Rule 823(c) and (d) to prepare and submit an annual compliance report to the Commission and to the SB SEF's Board. Based upon the Commission's estimates for similar annual reviews and reports by CCOs of investment companies, the Commission estimates that these reports would require an average of 92 hours per respondent per year.[534] Thus, the Commission estimates a total annual burden of 1,840 hours for all respondents.[535] Because the report would be submitted by the CCO, the Commission does not expect that the SB SEF would incur any external costs. The Commission solicits comments on the accuracy of its estimates.

A CCO would be required under proposed Rule 823(e)(1) and (2) and Exhibits F and H to proposed Form SB SEF to submit an annual financial report that would need to satisfy a number of requirements, including the requirement that a registered public accounting firm that is qualified and independent in accordance with Rule 2–01 of Regulation S–X (17 CFR 210.2–01) audit each financial report relating to the SB SEF (unaudited for certain affiliated entities). Based on conversations with operators of current trading platforms and the Commission's experience with entities of similar size, the Commission preliminarily estimates that the reports relating to the SB SEF generally would require, on average, 500 hours per respondent to complete and cost $500,000 for independent public accounting services per respondent. The Commission believes that the unaudited reports required for certain affiliated entities and available upon request by the Commission for other affiliated entities would not be overly time consuming to produce because, based on the Commission's experience with Form 1 filers, a respondent's accounting system should have this information available. Furthermore, because the information would not have to be audited, a respondent would only have to compile the information using a computer and commercially available software that it generally would own for pre-existing accounting purposes and then submit the information to the Commission. Based on the number of unaudited financial statements that the Commission receives from filers of Form 1 and the substance in these reports, the Commission estimates that it would take a SB SEF 40 hours to compile, review, and submit these reports. However, all of these reports would need to be provided in XBRL, as required in Rules 405(a)(1), (a)(3), (b), (c), (d) and (e) of Regulation S–T.[536] This would create an additional burden on respondents. The Commission preliminarily estimates that, based on its experience with other data tagging initiatives, these requirements would add an additional burden of an average of 54 hours and $23,000 in outside software and other costs per respondent per year. Thus, for purposes of complying with the financial statement requirements under proposed Rule 823(e)(1) and (2) and Exhibits F and H to proposed Form SB SEF, the Commission estimates a total annual burden of 11,880 hours [537] and $10,460,000 for respondents.[538] The Commission solicits comments as to the accuracy of this information.

As a result, the Commission estimates that the total burdens for compliance with proposed Rule 823 would be: (1) Initially, for the creation of the policies and procedures required in proposed Rule 823(b)(6) and (7), 160 hours and $40,000, per respondent, and 3,200 hours and $800,000, for all respondents; and (2) on an annual basis, for the annual compliance report and financial reports required under proposed Rule 823(c) through (e), 686 hours [539] and $523,000, per respondent, and 13,720 [540] hours and $10,460,000,[541] for all respondents.

The Commission preliminarily estimates that the total annual hourly burden for all SB SEFs combined for the CCO requirements in proposed Rule 823 would be 13,720 hours and the total one-time hourly burden would be 3,200. The Commission preliminarily estimates that the total annual cost burden for all SB SEFs to comply with the CCO requirements in proposed Rule 823 would be $10,460,000 and the total one-time cost burden would be $800,000.

8. Surveillance Systems Requirements for SB SEFs

As discussed above, proposed Rule 813(b) requires SB SEFs to have the capacity and resources to electronically monitor trading in SB swaps on its market by establishing an automated surveillance system, including through real-time monitoring of trading and use of automated alerts, to, among other things, detect and deter fraudulent or manipulative acts or practices, detect

Release No. IC–26299 (December 17, 2003); 68 FR 74714 (December 24, 2003) (adopting release) and *see* 2010 Extension of Rule 38a–1 Supporting Statement, Office of Management and Budget, available at: *http://www.reginfo.gov/public/do/PRAViewDocument?ref_nbr=201002-3235-028* ("ICA PRA"). The ICA PRA estimates a burden of 80 hours initially for the creation of such policies and procedures.

[530] 160 hours = 80 hours (burden per policy and procedure requirement) × 2 (number of policy and procedure requirements).

[531] 3,200 hours = 160 hours (initial burden per respondent) × 20 (number of SB SEF respondents).

[532] $40,000 = $400 (estimated hourly cost for outside counsel) × 50 hours (estimated amount of external legal work require per policy and procedure requirement) × 2 (number of policy and procedure requirements). The estimate of 50 hours of external legal work is from the Commission's estimate for external legal costs for complying with the requirements of Rule 611 of Regulation NMS for establishing polices and procedures thereunder. *See* Securities Exchange Act Release No. 51808 (June 9, 2005); 70 FR 37496 (June 29, 2005). *See also* 2008 Extension of Rule 611, Supporting Statement, Office of Management and Budget, available at: *http://www.reginfo.gov/public/do/PRAViewICR?ref_nbr=200802-3235-021*. The Commission preliminarily estimates an hourly cost of outside counsel at $400. *See* Municipal Securities Disclosure Release, *supra* note 438.

[533] $800,000 = $40,000 (initial burden per respondent) × 20 (number of SB SEF respondents).

[534] The ICA PRA estimated that CCOs of investment companies would expend 42 hours annually to conduct the annual review and prepare the annual compliance report under Rule 38a–1 under the ICA. *See* ICA PRA *supra* note 529. Because proposed Rule 823 would require slightly more than double the information that is required for CCO annual reports under Rule 38a–1, the Commission preliminarily estimates that the burden associated with the CCO's annual compliance report requirements of proposed Rule 823(c) and (d) would be 220% that of Rule 38a–1, which estimate would be approximately 92 hours.

[535] 1,840 hours = 92 hours (annual burden per respondent) × 20 (number of SB SEF respondents).

[536] *See* 17 CFR 232.405.

[537] 11,880 hours = 20 (number of SB SEF respondents) × 594 hours (500 hours for audited SB SEF financial statements + 40 hours for unaudited financial statements of affiliated entities + 54 hours for XBRL formatting of submission).s

[538] $10,460,000 = 20 (number of SB SEF respondents) × $523,000 ($500,000 for outside accounting services for auditing SB SEF's financial statements + $23,000 in outside software and other cost for formatting financial statement submission in XBRL format).

[539] 686 hours = 594 hours for financial report + 92 hours for annual compliance report.

[540] 13,720 hours = 686 hours (burden per respondent) × 20 (number of SB SEF respondents).

[541] $10,460,000 = 20 (number of SB SEF respondents) × $523,000 ($500,000 for outside accounting services for auditing SB SEF's financial statements + $23,000 in outside software and other cost for formatting financial statement submission in XBRL format).

and deter market distortions or disruptions of trading, conduct real-time monitoring of trading to provide for comprehensive and accurate trade reconstruction, and collect and assess data to allow SB SEFs to respond to market abuses and disruptions.[542]

Based on industry sources, the Commission preliminarily estimates that establishing an automated surveillance system would require one senior programmer and three additional programmers working for a year to create and implement such a system. Assuming a 1,800 hour work year, the Commission preliminarily estimates that the average one-time initial burden per respondent of establishing an automated surveillance system compliant with these requirements, would be 7,200 hours.[543] In addition, the Commission believes that a one-time capital expenditure of $1,500,000 in information technology costs would be necessary to establish such a system. This estimate is based on the Commission's discussions with market participants currently operating platforms that trade OTC swaps. Based on the estimated number of 20 SB SEF respondents, the Commission estimates a total start-up cost of 144,000 hours [544] and $30,000,000 in information technology costs.[545] Based on discussions with operators of current trading platforms, the Commission further estimates that to maintain these systems, a SB SEF would have to employ two programmer/analysts. Therefore, assuming a 1,800 hour work year, the Commission preliminarily estimates the average ongoing annual costs of these systems to be 3,600 hours per respondent [546] for a total of 72,000 hours for all respondents.[547] In addition, the Commission estimates that these systems may incur an ongoing information technology cost of and $500,000 per respondent, for a total ongoing annual burden of $10,000,000[548] The Commission solicits comments on the accuracy of its estimates.

9. Access by Non-Registered Eligible Contract Participants

As discussed above, proposed Rule 809(d)(1) would require a SB SEF that permits non-registered ECPs to be participants in the SB SEF to establish, document, and maintain a system of risk management controls and supervisory procedures reasonably designed to manage the financial, regulatory, and other risks of this business activity.[549] Proposed Rule 809(d)(2) would require that the risk management controls and supervisory procedures for granting access to certain ECPs as participants of the SB SEF be reasonably designed to ensure compliance with all regulatory requirements.[550] The Commission notes that proposed Rule 809(d) is modeled on recently adopted Rule 15c3–5 under Exchange Act.[551] The PRA analysis prepared in connection with that rule has informed the Commission's estimates of the paperwork burdens that would apply to SB SEFS under the proposed Rule 809(d).[552] Although the Commission reviewed the burden estimates it prepared in connection with Rule 15c3–5 to inform its burden estimates of the proposed Rule 809(d), the Commission recognizes that a number of entities that seek to become SB SEFs may not currently be regulated entities.

The Commission preliminarily believes that proposed Rule 809(d)(1) and (2) would impose a one-time collection of information burden on SB SEFs to establish or modify risk management systems, if they permit access by non-registered ECPs. The Commission preliminarily believes that the majority of entities that would seek to become SB SEFs would already have some risk management systems and supervisory procedures and controls to protect the integrity of their business and to comply with other requirements already specified, analyzed and accounted for herein (*e.g.,* requirements relating to surveillance systems, recordkeeping, reporting, and the CCO). However, some entities that seek to become SB SEFs could have to change their systems and procedures and other entities that currently do not have such systems and procedures could have to establish new systems and procedures to comply with the requirement of proposed Rule 809(d).

The Commission preliminarily believes that each SB SEF would have a one-time burden to establish or modify its technology and systems to add the controls necessary to comply with the requirement of the proposed Rule 809(d). The Commission estimates that each SB SEF would spend an average of 225 hours to develop or modify their systems to bring them into compliance with the proposed rule for a total one-time burden for all SB SEFs combined of 4,500 hours.[553] Based on industry sources, the Commission preliminarily believes that the development or modification of the required technology and systems would be performed internally.

The Commission also preliminarily believes that proposed Rules 809(d)(1) and (2) would impose an annual paperwork burden on each SB SEF to maintain its risk management system. The Commission preliminarily estimates that the ongoing annual burden for a SB SEF to maintain its risk management system would be 172.5 hours on average for a total annual burden for all SB SEFs combined of 3,450 hours.[554] The Commission believes that the ongoing burden of complying with the proposed rule's collection of information burden would include, among other things, updating systems to address any issues detected, updating risk management controls to reflect changes in the SB SEF's business model, and documenting and preserving its written description of risk management controls. Based on industry sources, the Commission preliminarily believes that the

[542] Proposed Rule 811(i) would require a SB SEF to have the capacity to capture information that may be used in establishing whether rule violations have occurred, including through the use of automated surveillance systems as set forth in proposed Rule 813(b). Proposed Rule 813(a)(2) would require a SB SEF to monitor trading in SB swaps to prevent manipulation, price distortion, and disruptions of the delivery or cash settlement practices and procedures, including methods for conducting real-time monitoring of trading and comprehensive and accurate trade reconstructions. The Commission preliminarily believes that the information collection burden associated with these requirements would be included in the information collection burden for proposed Rule 813(b).

[543] 7,200 hours = 1,800 (initial hours burden per employee) × 4 (number of employees).

[544] 144,000 hours = 7,200 hours (initial burden per respondent) × 20 (number of SB SEF respondents).

[545] $30,000,000 = $1,500,000 (initial cost burden per respondent) × 20 (number of SB SEF respondents).

[546] 3,600 hours = 1,800 (annual hours burden per employee) × 2 (number of employees).

[547] 72,000 hours = 3,600 hours (annual burden per respondent) × 20 (number of SB SEF respondents).

[548] $10,000,000 = $500,000 (annual cost burden per respondent) × 20 (number of SB SEF respondents).

[549] *See* proposed Rule 809(d)(1).

[550] *See* proposed Rule 809(d)(2).

[551] *See* 17 CFR.240.15c3–5. Though the Commission is relying on the PRA estimates it prepared in connection with Rule 15c3–5 to inform its PRA estimates for this proposed rule, the Commission notes that some of the specific requirements, controls and procedures in Rule 15c3–5 are not contained in the proposed Rule 809(d) for SB SEFs.

[552] *See* Securities Exchange Act Release No. 63241 (November 3, 2010), 75 FR 69792 (November 15, 2010).

[553] 4,500 hours = 225 (estimated average one-time burden to set up or modify systems to comply with collection of information under proposed Rule 809(d)) × 20 (number of SB SEF respondents).

[554] 3,450 hours = 225 hours (estimated average annual burden to establish or maintain risk management systems to comply with collection of information under proposed Rule 809(d)) × 20 (number of SB SEF respondents).

maintenance of a SB SEF's risk management systems would performed internally by one or more programmers.

The Commission preliminarily believes that proposed Rule 809(d) would impose a one-time legal and compliance burden on each SB SEF to comply with the requirement to establish, document, and maintain risk management controls and supervisory procedures. Based on the Commission's experience with broker-dealers and ATSs, the Commission preliminarily estimates that the average initial one-time legal and compliance burden would be approximately 52.5 hours per SB SEF for a total one-time legal and compliance burden for all SB SEFs combined of 1,050 hours.[555] The Commission preliminarily estimates that one internal compliance attorney and one internal compliance manager would spend on average 7.5 hours each to evaluate appropriate access controls and procedures. The Commission also preliminarily estimates that one internal compliance attorney and one compliance manager would each require approximately 15 hours, and the CCO would require approximately 7.5 hours, to set up or modify compliance policies and procedures to comply with the proposed rule, which includes establishing written policies and procedures for reviewing the overall effectiveness of risk management controls and supervisory procedures.

The Commission also preliminarily believes that proposed Rule 809(d) would impose an annual paperwork burden on SB SEFs to review and document their written risk management controls and supervisory procedures. Based on the Commission's experience with broker-dealers and ATSs, the Commission believes that a SB SEF's ongoing annual burden would be approximately 75 hours on average for a total annual burden for all SB SEFs combined of 1,500 hours.[556] This estimate includes an average of 30 hours per year for each of an internal compliance attorney and compliance manager, and 15 hours per year for the CCO, to review, document and updated these policies and procedures.

Therefore, the Commission preliminarily estimates that the total one-time burden for all SB SEFs to comply with the collection of information requirements of proposed Rule 809(d) would be 5,550 hours[557] and the total annual burden to comply with the proposed Rule would be 4,950 hours.[558]

10. Composite Indicative Quote and Executable Bids and Offers

Proposed Rule 811(e) would require a SB SEF that operates an RFQ platform to create and disseminate through the SB SEF a composite indicative quote, made available to all participants, for SB swaps traded on or through the SB SEF and the Commission's proposed interpretation of SB SEF would require each SB SEF, at the minimum, to provide any participant with the ability to make and display executable bids or offers accessible to all participants on the SB SEF, if the participant wishes to do so. The Commission preliminarily believes that most if not all of the respondents that operate RFQ platforms already have systems that collect and disseminate a composite indicative quote for other securities traded on or through the respondents' platforms. The Commission also preliminarily believes that SB SEFs currently have the capability to offer the executable bids and offers function to its participants. Thus, the Commission preliminarily believes that the composite indicative quote and the executable bids and offers requirements would result in little or no collection of information burden for such entities. The Commission recognizes, however, that some SB SEFs may have a one-time burden to establish or update their systems to collect and disseminate composite indicative quote information and to offer the executable bids and offers function and an ongoing annual burden to determine that such composite indicative quote mechanisms and executable bids and offers function are operating properly. The Commission does not know how many SB SEFs would have to establish or update their systems to collect and disseminate composite indicative quote information or to provide the executable bids and offer function. Therefore, for PRA purposes the Commission estimates that all of the estimated 20 SB SEF respondents would incur the paperwork burdens associated with these requirements.

The Commission preliminarily believes that this work would be performed internally by one senior programmer and one programmer. The Commission preliminarily believes that one senior programmer and one programmer would spend approximately 40 hours each to establish or update the SB SEF's systems to include the composite indicative quote and executable bids and offers functions. The total one-time burden, on average, for a SB SEF to establish or update its system to include these functions would be 80 hours for a total one-time burden for all SB SEFs combined of 1,600 hours.[559] Further, the Commission preliminarily believes that one programmer would spend approximately 50 hours annually, on average, monitoring and updating the system to determine that the composite indicative quote and the executable bids and offers functions would be operating appropriately. The total annual burden to all SB SEFs combined for monitoring and updating these mechanisms would be 1,000 hours.[560]

11. Total Paperwork Burden Under Regulation SB SEF

Based on the foregoing, the Commission preliminarily believes that the total one-time hourly burden for all SB SEFs and SB SEF participants combined pursuant to the requirements under Regulation SB SEF is equal to 264,801 hours[561] and $41,692,900.[562]

The Commission preliminarily believes that annual ongoing burden for all SB SEFs and SB SEF participants combined pursuant to the requirements

[555] 1,050 hours = 52.5 hours (estimated average one-time burden to establish, document, and maintain risk management controls and supervisory procedures to comply with collection of information under proposed Rule 809(d)) × 20 (number of SB SEF respondents).

[556] 1,500 hours = 75 hours (estimated average annual burden to establish, document, and maintain risk management controls and supervisory procedures to comply with collection of information under proposed Rules 809(d)(1) and (2)) × 20 (estimated number of SB SEF respondents).

[557] *See supra* notes 553 and 555 and accompanying text for calculations of total one-time burden to comply with collection of information under proposed Rules 809(d).

[558] *See supra* notes 554 and 556 and accompanying text for calculations of total annual burden to comply with collection of information under proposed Rules 809(d).

[559] 1,600 hours = 80 hours (estimated one-time collection of information burden to establish or update systems to comply with proposed Rule 811(e) and the Commission's proposed interpretation of the definition of SB SEF as it relates to executable bids and offers functions) × 20 (estimated number of SB SEF respondents).

[560] 1,000 hours = 50 hours (estimated annual collection of information burden to comply with proposed Rules 811(e)) × 20 (estimated number of SB SEF respondents).

[561] 263,201 hours = 13,901 hours (registration) + 4,400 hours (rule-writing) + 13,300 (SB SEF recordkeeping) + 72,450 (SB SEF participant recordkeeping) + 6,400 (timely publication of trading information) + 3,200 (CCO requirements) + 144,000 (surveillance systems) + 5,550 (access by ECPs) + 1,600 (composite indicative quote).

[562] $41,692,900 = $10,478,900 (registration) + $36,000 (SB SEF recordkeeping) + $378,000 (SB SEF participant recordkeeping) + $800,000 (CCO requirements) + $30,000,000 (surveillance systems).

under Regulation SB SEF are equal to 165,632 hours [563] and $22,342,700.[564]

E. Collection of Information Is Mandatory

The collections of information pursuant to Regulation SB SEF would be mandatory for all registered SB SEFs and SB SEF participants, as applicable.

F. Responses to Collection of Information Will Not Be Confidential

Other than information for which a SB SEF or a SB SEF participant requests confidential treatment, or as may otherwise be kept confidential by the Commission, and which may be withheld from the public in accordance with the provisions of the Freedom of Information Act ("FOIA"), 5 U.S.C. 522, the collection of information pursuant to the proposed rules would not be confidential and would be publicly available.

G. Retention Period of Recordkeeping Requirements

Although recordkeeping and retention requirements have not yet been established for SB SEFs under the Exchange Act provisions added by the Dodd-Frank Act, the Commission is authorized to adopt such rules under proposed Regulation SB SEF as part of this proposed rulemaking.[565] Proposed Rule 818 under Regulation SB SEF would require a SB SEF to maintain records of all documents made or received by it in the conduct of its business for a period of not less than five years, the first two years in an easily accessible place.

H. Request for Comment

Pursuant to 44 U.S.C. 3505(c)(2)(B), the Commission solicits comment to:

1. Evaluate whether the proposed collection of information is necessary for the performance of the functions of the agency, including whether the information shall have practical utility;

2. Evaluate the accuracy of the agency's estimate of the burden of the proposed collection of information;

3. Determine whether there are ways to enhance the quality, utility, and clarity of the information to be collected; and

4. 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 wishing to submit comments on the collection of information requirements should direct them to the following persons: (1) Desk Officer for the Securities and Exchange Commission, Office of Information and Regulatory Affairs, OMB, Room 3208, New Executive Office Building, Washington, DC 20503; and (2) Secretary, Securities and Exchange Commission, Station Place, 100 F Street, NE., Washington, DC 20549–1090 with reference to File No. S7–06–11. OMB is required to make a decision concerning the collection of information between 30 and 60 days after publication, so a comment to OMB is best assured of having its full effect if OMB receives it within 30 days of publication. The Commission has submitted the proposed collection of information to OMB for approval. Requests for the materials submitted to OMB by the Commission with regard to this collection of information should be in writing, refer to File No. S7–06–11, and be submitted to the Securities and Exchange Commission, Office of Investor Education and Advocacy, Station Place, 100 F Street, NE., Washington, DC 20549–0213.

XXVIII. Consideration of Costs and Benefits

A. Overview

To increase the transparency and oversight of the OTC derivatives market, Title VII of the Dodd-Frank Act requires the Commission to undertake a number of rulemakings to implement the regulatory framework for SB swaps that is set forth in the legislation, including the registration and regulation of SB SEFs.[566] Pursuant to Section 763(c) of the Dodd-Frank Act, the Commission is required to adopt rules providing for: (1) The registration and regulation of SB SEFs; and (2) the compliance by SB SEFs with the Core Principles set forth thereunder.[567] To satisfy this statutory mandate, the Commission is proposing Regulation SB SEF, which would contain several rules setting forth the requirements for a platform or system to register with the Commission, and to maintain that registration, as a SB SEF, and Form SB SEF, which would contain the application form and the materials that an applicant would have to provide as part of the registration process. In addition, proposed Regulation SB SEF would contain a series of rules that are designed to implement the 14 Core Principles with which a SB SEF is statutorily required to comply. The proposed registration form and rules contained in Regulation SB SEF are designed to promote the goals of the Dodd-Frank Act of having SB swaps trade on a regulated market. In conjunction with other rulemakings proposed by the Commission under the Dodd-Frank Act, including rule proposals relating to SB swap trade reporting,[568] SB swap data repositories,[569] the mitigation of conflicts of interest relating to SB SEFs, SBS exchanges and SB swap clearing agencies,[570] and SB swap anti-fraud and anti-manipulation prohibitions,[571] the proposed registration form and rules governing SB SEFs are intended to lead to a more robust, transparent, and competitive environment for the market for SB swaps.

Currently, SB swaps trade in the OTC market, rather than on regulated markets. The existing market for SB swaps is opaque, with little, if any, pre-trade or post-trade transparency. A key goal of the Dodd-Frank Act is to bring more transparency to the OTC derivatives markets and to bring the trading of SB swaps onto regulated markets.[572] The Commission, in drafting rules to implement the SB SEF provisions of the Dodd-Frank Act, is proposing to put in place a regulatory structure that will foster a transparent, fair, and competitive market for the

[563] 164,632 hours = 3,154 (registration) + 2,400 hours (rule-writing) + 24,208 hours (SB SEF reporting) + 27,500 hours (SB SEF participant reporting) + 3,600 hours (SB SEF recordkeeping) + 8,400 hours (SB SEF participant recordkeeping) + 4,700 hours (rule and product filings) + 13,720 hours (CCO requirements) + 72,000 hours (surveillance systems) + 4,950 (access by ECPs) + 1,000 (composite indicative quote).

[564] $22,342,700 = $2,700 (registration) + $1,880,000 (SB SEF reporting) + $10,460,000 (CCO requirements) + $10,000,000 (surveillance systems).

[565] As discussed above, new Section 3D of the Exchange Act sets forth 14 Core Principles that a SB SEF would need to satisfy, including one relating to recordkeeping and reporting, and provides the Commission with rulemaking authority with respect to implementation of these Core Principles. *See* Public Law 111–203, § 763(c) (adding Section 3D of the Exchange Act).

[566] *See* Public Law 111–203 Preamble.

[567] The Core Principles applicable to SB SEFs are captioned: (1) Compliance with Core Principles; (2) Compliance with Rules; (3) Security-Based Swaps Not Readily Susceptible to Manipulation; (4) Monitoring of Trading and Trade Processing; (5) Ability to Obtain Information; (6) Financial Integrity of Transactions; (7) Emergency Authority; (8) Timely Publication of Trading Information; (9) Recordkeeping and Reporting; (10) Antitrust Considerations; (11) Conflicts of Interest; (12) Financial Resources; (13) System Safeguards; and (14) Designation of Chief Compliance Officer.

[568] *See* Reporting and Dissemination Release, *supra* note 6.

[569] *See* SDR Release, *supra* note 6.

[570] *See* Regulation MC Proposing Release, *supra* note 82.

[571] *See* Prohibition Against Fraud, Manipulation, and Deception in Connection with Security-Based Swaps, Exchange Act Rel. No. 63236, proposed on Nov. 3, 2010.

[572] *See* Public Law 111–203 Preamble. *See also* Section 3C(h) of the Exchange Act, Public Law 111–203, requiring that, subject to certain exceptions, any SB swap subject to mandatory clearing must be traded on a SB SEF or an exchange.

trading of SB swaps. Considering the early stage of regulatory development and the existing structure of the SB swaps market, however, the Commission is mindful that the proposed rules could have unforeseen consequences, either beneficial or undesirable, with respect to the shape that this market will take. In the Commission's view, it is important that the regulatory structure provides incentives for the trading of SB swaps on regulated markets that are designed to foster greater transparency and competition and are subject to Commission oversight, while at the same time allowing for the continued efficient innovation and evolution of the SB swaps market. In this regard, rather than proposing a rule that establishes a prescribed format for the system or platform that constitutes a SB SEF, the Commission is proposing to provide baseline principles, consistent with the requirements of the Exchange Act, that any potential SB SEF would need to meet as a condition to registration as a SB SEF. Such an approach would allow flexibility to those trading venues that plan to register as SB SEFs and would permit the continued development of organized markets for the trading of SB swaps. This more flexible approach also would allow the Commission to monitor the market for SB swaps and propose adjustments, as necessary, as this market evolves.

The Commission believes that the proposed registration form and rules under Regulation SB SEF would create a comprehensive structure for the registration and regulation of SB SEFs, but would also impose costs on market participants. The Commission is sensitive to the costs and benefits that would result from proposed Regulation SB SEF and has identified certain costs and benefits of these proposals, as described more fully below. The Commission requests comment on the costs and benefits associated with the proposed registration form and rules contained in proposed Regulation SB SEF, and its cost-benefit analysis thereof, including identification and assessments of any costs and benefits not discussed in this analysis. The Commission also seeks comment on the accuracy of any of the benefits and costs it has identified below and also welcomes comments on the accuracy of any of its cost estimates. Finally, the Commission encourages commenters to identify, discuss, analyze, and supply relevant data, information, or statistics regarding any such costs or benefits.

Because the structure of the SB swaps market and the behavior of its market participants is likely to change after the effective date of the Dodd-Frank Act and implementation of the Commission's rules promulgated thereunder, the impact of—and the costs and benefits that may result from—proposed Regulation SB SEF may change over time. As commenters review proposed Regulation SB SEF, they are urged to consider generally the role that regulation may play in fostering or limiting the development of the market for SB swaps.

B. Benefits

SB SEFs are expected to play a critical role in enhancing the pre-trade transparency and oversight of the market for SB swaps. SB SEFs should help further the statutory objective of financial stability and greater transparency for SB swaps [573] by providing a venue for counterparties to execute trades in SB swaps and also by serving as a conduit for information regarding trading interest in SB swaps. In addition, because the proposed rules would impose certain regulatory responsibilities on SB SEFs, such as monitoring trading, assuring the ability to obtain information, and establishing and enforcing rules and procedures to ensure the financial integrity of SB swaps entered on or though the SB SEF, SB SEFs would be charged with an important role in helping to oversee trading in the market for SB swaps on an ongoing basis and allowing regulators to quickly assess information regarding the potential for systemic risk across trading venues.

Broadly, the Commission anticipates that Regulation SB SEF may bring several overarching benefits to the SB swap market. These include the following:

Improved Transparency. The proposed rules on the registration and regulation of SB SEFs could have significant benefits to the market for SB swaps. The trading of SB swaps on regulated markets, *i.e.,* SB SEFs, should bring more transparency to the currently opaque market for SB swaps. In addition, the Commission's proposed interpretation of the definition of a SB SEF, combined with the proposed rules relating to pre-trade transparency, should increase overall transparency in the market for SB swaps. Increased pre-trade price transparency should help alleviate informational asymmetries that may exist today in the SB swaps markets and allow an increased number of market participants to be able to see the trading interest of other market participants prior to trading, which should lead to increased price competition among market participants.[574] The Commission preliminarily believes that the proposed requirements with respect to pre-trade price transparency should lead to more efficient pricing in the SB swaps market,[575] but is mindful that, under certain circumstances, pre-trade price transparency could also discourage the provision of liquidity by some market participants.[576]

The Commission preliminarily believes that proposed Rule 811(e), which would require a SB SEF that operates an RFQ platform to create and disseminate through the SB SEF a composite indicative quote, made available to all participants, for SB swaps traded on or through the SB SEF, would provide a certain level of pre-trade transparency for an RFQ platform. Displaying the composite indicative quote would include displaying both composite indicative bids and composite indicative offers for SB swaps traded on or through the SB SEF. As a result of this proposal, an average indicative pricing interest would be available to all of the SB SEF's participants. The Commission also believes that including RFQ responses in the composite indicative quote would be an appropriate method to inform SB SEF participants of changes in the average level of pricing interest due to responses.[577] At the same time, the dissemination of a composite indicative quote would provide a greater level of anonymity for the execution of trades on an RFQ platform compared with the dissemination of an individual participant's indications of interest or responses to an RFQ.

In addition, the Commission preliminary believes that proposed Rule 817(c), which prohibits a SB SEF from making any information regarding a SB swap transaction publicly available prior to the time that a SDR would be permitted to disseminate the trade information, could positively impact the market for block trades. Under proposed Rule 817(c), a SB SEF could not

[573] *See* Public Law 111–203 Preamble.

[574] *See, e.g.,* Ananth Madhavan, *Market Microstructure: A Practitioner's Guide,* Fin. Analysts J., Vol. 58, at 38 (2002) (nondisclosure of pre-trade price information benefits dealers by reducing price competition).

[575] *See, e.g.,* Ekkehart Boehmer, *et al., Lifting the Veil: An Analysis of Pre-trade Transparency at the NYSE,* J. of Fin., Vol. LX (2005) (greater pre-trade price transparency leads to more efficient pricing).

[576] *See, e.g.,* Ananth Madhavan, *et al., Should Securities Markets Be Transparent?* J. of Fin. Markets, Vol. 8 (2005) (finding that an increase in pre-trade price transparency leads to lower liquidity and higher execution costs, because limit-order traders are reluctant to submit orders given that their orders essentially represent free options to other traders).

[577] *See supra* Section VIII.C.1.

publicly disseminate complete transaction reports for block trades (*i.e.,* including the transaction ID and the full notional size) prior to the time SDRs would be permitted to do so. The Commission believes that proposed Rule 817(c) would provide parties to block trades some flexibility in timing their transactions. Based on discussions with market participants, the Commission believes that parties to block trades favor a consistent approach to the timing of the public reporting of such trades. Therefore, the Commission preliminary believes that parties to block trades, especially dealers, would be able to have more flexibility in effecting a block trade and any associated hedging transactions, because trade information about the block could not be made publicly available by the SB SEF prior to the time that it is permitted to be disseminated by a SDR.[578] Furthermore, if the market participants choose to utilize this functionality, the display of executable bids or offers should also improve pre-trade price transparency.

Improved Oversight. The proposed rules would require SB SEFs to maintain an audit trail and surveillance systems to monitor trading. Regulation SB SEF also would require comprehensive reporting and recordkeeping by SB SEFs. These requirements would put in place a structure that would provide the SB SEF with information to better enable it to oversee trading on its market by its participants, including detecting and deterring fraudulent and manipulative acts. Regulation SB SEF would also provide the Commission with greater access to information on the trading of SB swaps to support its responsibilities to oversee the SB swaps market. Further, Regulation SB SEF would enable the Commission to share that information with other Federal financial regulators in instances of broad market turmoil.

This framework could in turn lead to increased confidence in a well-regulated market among SB swaps market participants. To the extent market participants consider a well-regulated market as significant to their investment decisions, trust, which is a component of investor confidence, is improved and market participants may be more willing to participate in the SB swaps market. An increase in participation in the SB swaps market can potentially benefit the SB swaps market as a whole. Further, to the extent that market participants utilize SB swaps to better manage their risk with respect to a position in underlying securities or assets, the extent they are willing to participate in the SB swaps market may impact their willingness to participate in the underlying asset's market. Thus, the Commission preliminarily believes that the proposal could benefit the securities markets overall by encouraging a more efficient, and potentially higher, level of capital investment.

Improved Access and Competition. Currently, the market for SB swaps is dominated by a small group of dealers.[579] The Dodd-Frank Act's mandate to bring SB swaps that are subject to the mandatory clearing requirement onto regulated markets, unless the SB swap is not made available to trade,[580] and proposed Regulation SB SEF, which is intended to help implement the statutory directive, should help foster greater competition in the trading of SB swaps by increasing access to SB swap trading venues. The proposed rules would provide a framework to allow a number of trading platforms or systems to register as SB SEFs and thus more effectively compete for business in SB swaps. Proposed Rule 809(b) would require a SB SEF's rules to permit all eligible persons that meet the requirements for becoming a participant as set forth in the SB SEF's rules to become participants in the SB SEF.[581] Proposed Rule 809(b) would also give a SB SEF the option to not permit any non-registered ECP to become participants in the SB SEF. As such, proposed Rule 809(b) provides SB SEFs with flexibility in choosing whether or not to provide access to non-registered ECPs. Proposed Rule 809(d) would require that, if a SB SEF chooses to permit non-registered ECPs to become participants, it would be responsible for establishing risk management controls and supervisory procedures reasonably designed to manage financial, regulatory, and other risks associated with the non-registered ECP's access. These proposed requirements should reduce risks associated with access to SB SEFs by non-registered ECPs (*e.g.,* if they enter into trades that exceed appropriate credit or capital limits or submit erroneous orders). In addition, the Commission preliminarily believes that a SB SEF is best positioned to implement the proposed controls and procedures.

Proposed Rule 811(b)(1) would require every SB SEF to establish fair, objective and not unreasonably discriminatory standards for granting impartial access to trading on the SB SEF. In addition, proposed Rule 811(b)(3)–(4) would require every SB SEF to make and keep records of all denials, or limitations, of access to the SB SEF, and to report such information to the Commission. These proposed requirements would further the requirement in the Exchange Act that SB SEFs provide market participants with impartial access.[582] Taken together, these proposed rules should foster greater direct access to SB SEFs by dealers, major SB swap participants, brokers and ECPs. This impartial access should, in turn, promote greater participation by liquidity providers and competition on each SB SEF. Increased participation could lead to reduced information asymmetries among market participants, while increased competition could lead to more efficient and better pricing in the SB swaps market. Further, a more competitive environment should lead to lower trading costs, which may lead to increased participation in the SB swaps market. Impartial access requirements also would help guard against situations where certain participants in a SB SEF (who also might be owners of the SB SEF) might seek to limit the number of other participants in the SB SEF in order to limit competition and increase their own profits. Thus, the impartial access should, in turn, promote greater participation by liquidity providers and competition on each SB SEF.

As proposed, SB SEFs would remain free to establish standards for impartial access consistent with the requirement that they be fair and objective and do not unfairly discriminate, and that they do not apply the standards in an unfair or unreasonably discriminatory manner. Therefore, SB SEFs could choose the most cost-effective methods to ensure that all their participants and would-be participants are evaluated on a fair and impartial basis.

To address the problem of restricting the scope of SB swaps that trade on SB SEFs, the Commission is proposing to require that each SB SEF have a swap review committee that would determine which SB swaps would trade on the SB SEF, as well as the SB swaps that should no longer trade on the SB

[578] *See* Reporting and Dissemination Release, *supra* note 6, and proposed Rule 904(d) of Regulation SBSR. *See also* proposed Rule 817(c) of Regulation SB SEF.

[579] *See supra* note 81.

[580] *See* Section 3C(h) of the Exchange Act.

[581] Proposed Rule 809(a) would require SB SEFs to only permit a person to become a participant in the security-based swap execution facility if such person is registered with the Commission as a security-based swap dealer, major security-based swap participant, or broker (as defined in section 3(a)(4) of the Act, 15 U.S.C. 78c(a)(4)), or if such person is an eligible contract participant (as defined in section 3(a)(65) of the Act, 15 U.S.C. 78c(a)(65)).

[582] *See* Section 3D(d)(2)(B)(i) of the Exchange Act.

SEF.[583] Proposed Rule 811(c)(2) would require that the composition of the swap review committee must provide for the fair representation of participants of the SB SEF as well as other market participants such that each class of participant and other market participants would be given the right to participate in such swap review committee and that no single class of participant or category of market participant would predominate. Having a swap review committee that provides for the fair representation of participants and other market participants should help assure that the process of determining those SB swaps that should trade on the SB SEF would be fair and that various classes of participants in the SB SEF, as well as other market participants, would have a voice in those decisions.

Consequently, the Commission believes that the proposed rules requiring impartial access to trading on the SB SEF and providing for fair representation on the swap review committee to determine which SB swaps should be traded on SB SEFs should help mitigate the inappropriate exercise of market power by any given market participant or group of market participants. In addition, the Commission believes that, in a competitive market, new SB SEFs could be created to attract market participants that are unable to meet the objective requirements of more exclusive SB SEFs or to trade the SB swaps other SB SEFs decide not to trade.

The Commission also believes that its proposed interpretation of which facilities fall within the term SB SEF, providing, at the minimum, any participant with the ability to make and display executable bids or offers accessible to all participants on the SB SEF, if the market participant wishes to do so, would also improve access to the SB SEF by participants because it provides participants an additional method with which to execute transactions on the SB SEF.

Improved Commission and SB SEF Oversight. The Commission believes that one of the goals of the Dodd-Frank Act is to increase the regulatory oversight over the currently unregulated OTC derivative markets.[584] Proposed Regulation SB SEF would provide the means for the Commission to gain better insight into and oversight of the market for SB swaps. The proposed rules would provide the Commission the ability to, among other things, review the rules of SB SEFs, obtain data and records from SB SEFs, and inspect and examine SB SEFs, all of which would support the Commission's oversight function over the SB swaps market, as directed by Congress in the Dodd-Frank Act.

Specifically, proposed Rule 818(a) would require each SB SEF to keep and preserve all documents, including all correspondence, memoranda, papers, books, notices, accounts, and other such records that would be made or received by it in the conduct of its business. In addition, proposed Rule 818(c) would require SB SEFs to keep audit trail records relating to all orders, requests for quotations, responses, quotations, other trading interest, and transactions that are received by, originated on, or executed on, the SB SEF. The records required to be kept, preserved and maintained by a SB SEF under proposed Rule 818 would help the Commission to determine whether an SB SEF is operating in compliance with the Exchange Act and the rules and regulations thereunder. The audit trail information required to be maintained under proposed Rule 818(c) would facilitate the ability of the SB SEF and the Commission to carry out their respective obligations under the Exchange Act, by providing a record of the complete history of all trading interest entered and transactions executed on the SB SEF. This audit trail could be used to help detect abusive or manipulative trading activity, prepare reconstructions of activity on the SB SEF or in the SB swaps market, and generally to understand the causes of unusual market activity.

Furthermore, proposed Rule 811(h) would require the SB SEF to make and keep records specifically of all disciplinary proceedings and appeals, which would allow the Commission to review the disciplinary process at a SB SEF, providing the Commission an additional tool to carry out its oversight responsibilities. The proposed registration requirements and related proposed Form SB SEF, and the CCO's annual compliance report, which are further discussed below, should also aid the Commission in its oversight responsibilities. As a whole, proposed Regulation SB SEF should facilitate the Commission's work in preparing the semi-annual and annual public reports of SB swap data required by Section 763 of the Dodd-Frank Act, because the Commission would be able to obtain information about the SB swap market through its oversight of SB SEFs.[585]

Improved Automation. In order to comply with the requirements of proposed Regulation SB SEF relating to recordkeeping and surveillance, SB SEFs would need to invest in and develop automated technology systems to store, monitor and communicate a variety of trading data, including orders, requests for quotations, responses and quotations, among others. The Commission preliminary believes that the proposed rules should bring about increased automation in the SB swaps markets. This increased automation could help market participants more efficiently track their trading and risk exposures in SB swaps. In addition, the automation and systems development associated with the regulation of SB SEFs, as required by proposed Regulation SB SEF, could provide SB swaps market participants with new platforms and tools to execute and process transactions in SB swaps at a lower expense per transaction. Such increased efficiency would enable participants of the SB SEF to handle increased volumes of SB swaps with greater efficiency.

In addition to the broad benefits that the Commission anticipates that Regulation SB SEF may bring to the SB swaps market, the Commission preliminarily believes that its individual proposed rules may bring particular benefits to the SB swap market. These include the following:

Interpretation of SB SEF Definition. The Commission believes that its proposed interpretation of the scope of the definition of SB SEF[586] should provide sufficient flexibility for market participants in creating and operating a variety of SB SEFs to trade SB swaps. The Commission preliminary believes that a system or a platform which allows a participant the ability to send an RFQ to *all* participants, as well as the choice to send an RFQ to fewer than all participants, would provide flexibility to the market, because participants would be able to trade SB swaps by accepting bids and offers from multiple participants, while still preserving the ability of each participant to decide how

[583] *See* proposed Rule 811(c). *See also* Core Principle 3 and proposed Rule 812, which permit a SB SEF to trade only SB swaps that are not readily susceptible to manipulation. Prior to trading any SB swap, proposed Rule 812 would require the swap review committee to determine whether, after taking into account all of the terms and conditions of the SB swap and the markets for the SB swap and any underlying security or securities, that such SB swap is not readily susceptible to manipulation. Proposed Rule 812 also would require the swap review committee to periodically review that determination.

[584] *See* Public Law 111–203 Preamble.

[585] *See* Section 763(i) of the Dodd-Frank Act requiring the Commission to provide SB swap data to the public.

[586] *See supra* Section III.B for a detailed discussion of the proposed interpretation of the definition of SB SEF.

broadly or narrowly to disseminate his or her RFQ.

The Commission believes that this proposed interpretation would likely encourage a greater number of SB swaps to trade on SB SEFs because, as mentioned above, it would give requestors the flexibility to determine how best to broadcast their interests.

The Commission believes that, rather than proposing a rule that establishes a prescribed format for a system or platform that constitutes a SB SEF, the better approach is to provide baseline principles, as outlined in the proposed interpretation consistent with the requirements of the Exchange Act, that any potential SB SEF would need to meet as a condition to registration as a SB SEF. Such an approach should provide flexibility to those trading venues that plan to register as SB SEFs and would permit the continued development of organized markets for the trading of SB swaps.

Exemptions from Definition of Exchange and Certain Regulatory Requirements Applicable to a Broker. The proposed rules would include exemptions for SB SEFs from the definition of "exchange" and from most regulations governing brokers. Using its exemptive authority under Section 36 of the Exchange Act, the Commission is proposing: (1) To amend Rule 3a1–1 under the Exchange Act to exempt any SB SEF from the definition of "exchange," if such SB SEF provides a marketplace solely for the trading of security-based swaps (and no other security) and complies with the provisions of proposed Regulation SB SEF;[587] and (2) new Rule 15a–12 to allow a person that meets the definition of a SB SEF and broker, to satisfy the broker registration requirements by registering as a SB SEF. The Commission believes that Congress specifically provided a comprehensive regulatory framework for SB SEFs in the Dodd-Frank Act and, therefore, SB SEFs should not also be required to be regulated as national securities exchanges or as brokers. Without these proposed exemptions, SB SEFs would be required to register with the Commission not only as SB SEFs, but also as exchanges and brokers. Given the regulatory framework for SB SEFs required by the Exchange Act and proposed Regulation SB SEF, the Commission preliminarily believes that requiring a SB SEF to register in such multiple capacities would not be efficient. The Commission believes that reducing or eliminating such inefficiency will confer an overall benefit to the SB swaps market by reducing the costs of complying with unnecessary rules or regulations.

Registration. The registration of SB SEFs is a requirement under the Dodd-Frank Act.[588] Proposed Rule 810(a) incorporates the requirement under the Dodd-Frank Act that a SB SEF, in order to be registered and maintain registration, comply with the Core Principles in Section 3D(d) of the Exchange Act and any requirement that the Commission may impose by rule or regulation. The proposed registration process is intended to implement this requirement and assist the Commission in overseeing and regulating the SB swaps market. The information to be provided on proposed Form SB SEF is designed to enable the Commission to assess whether an applicant has the capacity and the means to perform the duties of a SB SEF and to comply with the Core Principles and other requirements imposed on registered SB SEFs.

In addition, the amendments, supplemental information and notices that the Commission proposes to require registered SB SEFs to file pursuant to proposed Rules 802, 803 and 804 are designed to further the ability of the Commission to efficiently monitor SB SEFs' compliance with the provisions of the Exchange Act and to oversee the marketplace for SB swaps and, specifically, the trading of SB swaps on SB SEFs.

Rule and Product Filings. Proposed Rules 805 and 806 set forth two alternative filing processes for a new rule or rule amendment of a registered SB SEF, and proposed Rules 807 and 808 set forth two alternative filing processes for SB SEFs to submit filings for new products that it trades. The proposed rules are intended to assist the Commission in overseeing and regulating the trading of SB swaps and to help ensure that SB SEFs operate in compliance with the Exchange Act. The self-certification processes of Rules 806 and 807 require SB SEFs to include a certification that the proposed new rule or rule amendment or SB swap, as the case may be, complies with the Exchange Act and Commission rules and regulations thereunder.[589]

The information to be provided by the SB SEF under proposed Rules 805 and 806 would further the ability of the Commission to assess whether a SB SEF has the capacity to perform the duties of a SB SEF and to comply with the duties, Core Principles, and other requirements imposed on registered SB SEFs, and to ensure that a registered SB SEF continues to comply with the requirements imposed on registered SB SEFs under the Exchange Act. In addition, proposed Rule 805(a)(4), which would require a SB SEF to explain the anticipated benefits and potential anticompetitive effects on market participants of a proposed new rule or rule amendment should help foster a competitive SB swaps market because it would require SB SEFs to disclose the positive as well as negative aspects of the SB SEF's proposed rules.

The information to be provided by the SB SEF under proposed Rules 807 and 808 would further the ability of the Commission to obtain information regarding SB swaps that a SB SEF intends to trade on its market. In addition, because these processes are comparable to the parallel processes of the CFTC, they would promote efficiency for SB SEFs that are also registered as SEFs.

Chief Compliance Officer. The submission of the CCO's annual compliance report and the annual financial report to the Commission as would be required by proposed Rule 823 would help the Commission monitor the compliance activities and financial state of SB SEFs. These reports would also assist the Commission in carrying out its oversight of the SB SEFs and the SB swaps market by providing the Commission the information necessary to review instances, for example, of non-compliance and denials of access.

Conflicts of Interest. Proposed Rule 820 sets forth certain governance arrangements that would be required of SB SEFs. Proposed Rule 820(a) would require the rules of a SB SEF to assure a fair representation of its participants in the selection of its directors and administration of its affairs. No less than 20% of the total number of directors of the SB SEF would be required to be selected by the SB SEF participants. Further, the Commission proposes that SB SEF participant owners be restricted in their ability to participate in the "fair representation" process. In addition, proposed Rule 820(b) would require that at least one director on the Board be representative of investors ("investor director") who are (1) not SB swap dealers or major SB swap participants and (2) not associated with a participant. Finally, proposed Rule 820(c) would require the rules of a SB SEF to establish a fair process for SB SEF participants to nominate an alternative candidate or candidates to the Board by petition.

[587] *See* proposed Rule 3a1–1(a)(4).

[588] *See* Section 3D(a)(1) of the Exchange Act.

[589] *See* proposed Rules 806(a)(5)(iii) and 807(a)(4)(iii).

The requirements of proposed Rule 820 are important to help ensure that SB SEF participants and investors have a voice in the administration and governance of the SB SEF, without jeopardizing the overall independence of the Board.[590] The proposed governance requirements should also help to mitigate any conflicts of interest that may arise between SB SEF participants who also could be owners of the SB SEF, by reducing the possibility that a small group of market participants would have the ability to unfairly disadvantage other market participants through the SB SEF governance process. In order to further mitigate conflicts of interest and achieve fairness in the governance process of a SB SEF, the proposal would also provide for the ability of SB SEF participants to have alternative candidates by requiring the SB SEF to establish a fair process for SB SEFs to nominate an alternative candidate or candidates by petition. Finally, the Commission believes that requiring representation on the SB SEF Board by investors who are not SB swap dealers or major SB swap participants, or associated with SB SEF participants, would provide an important perspective to the governance and administration of a SB SEF. Investor directors could provide unique and different perspectives from dealers and other participants of the SB SEF, which should enhance the ability of the Board to address issues in an impartial fashion and consequently support the integrity of a SB SEF's governance.

C. Costs

Although the Commission believes that proposed Regulation SB SEF would result in significant benefits to the market for SB swaps, the Commission recognizes that the proposed registration form and rules would also entail significant costs. Some costs are difficult to precisely quantify and are discussed below.

The Commission is mindful that any rules it may adopt with respect to SB SEFs under the Dodd-Frank Act may impact the incentives of market participants with respect to where and how they trade SB swaps. The Commission is cognizant that its proposed interpretation of the definition of SB SEF, coupled with the level of pre-trade transparency that would be required for trading on a SB SEF, will impact the development of the SB swaps market. Further, if the rules proposed by the Commission are, or are perceived to be, too costly for trading venues to comply with, fewer entities than expected may seek to register as SB SEFs, thus impacting competition. In addition, if the proposed rules for trading on a SB SEF are perceived as too burdensome by market participants, some trading of SB swaps may move to foreign markets whose regulations are perceived to be less restrictive, thus frustrating the goals of the Dodd-Frank Act. At the same time, if the proposed rules relating to SB SEFs are too lenient, they may have little or no impact on the market structure and surveillance of the SB swaps markets, which could result in the loss of many of the benefits discussed above and fail to achieve the goals of the Dodd-Frank Act of greater transparency. In addition, because the trading mechanisms in the OTC market will continue to be largely unregulated, OTC-traded SB swaps may be perceived by some market participants to be less expensive to trade than SB SEF-traded swaps, *i.e.,* in the sense that they are subject to less regulation.

In addition, SB swaps traded on SB SEFs may be perceived to be subject to increased costs, monetary and otherwise. For example, some industry participants have expressed their belief that any proposed requirement of pre-trade transparency would force market participants to reveal valuable economic information regarding their trading interest more broadly than they may believe would be economically prudent and could discourage participation in the SB swaps market. An additional impact of pre-trade transparency are perceived costs associated with front running, if customers or dealers are required to show their trading interest before a trade is executed. These potential costs of pre-trade transparency may change market participants' trading strategies, which could result in them working more orders or finding ways to attempt to hide their interest.[591] If market participants view the Commission's proposal as too burdensome with respect to pre-trade transparency, dealers may be less willing to supply liquidity for SB swaps that trade on SB SEFs or exchanges, thus impacting liquidity and competition. On the other hand, if the requirement with respect to pre-trade transparency is too loose, the result could be that there would be no substantive change from the status quo, including no benefits of alleviating informational asymmetries, increasing price competition and supplying better executions beyond the changes in response to the other requirements of Dodd-Frank. However, the Commission believes that this concern depends on the degree of pre-trade transparency required and the characteristics of the trading market. The proposed rules are intended to provide for greater pre-trade transparency than currently exists without requiring pre-trade transparency in a manner that would cause participants to avoid providing liquidity on SB SEFs.

The requirements of the proposed rules would impose the same minimum level of pre-trade transparency and order interaction on block trades as on non-block trades. This can potentially have an impact on the liquidity available on those types of platforms that would provide for block trading. Today, many block trades are transacted through voice brokerage, without pre-trade transparency and order interaction. Block trading enables, among other things, entities with large exposures to certain business risks to hedge those risks. For example, investors considering making investments in, or lenders considering making loans to, certain corporate borrowers may seek to purchase credit default swap ("CDS") protection to hedge some portion of the credit risk the investor does not want to retain. The availability of such credit risk protection in large block transaction size may therefore influence investment or lending decisions which in turn may influence the cost of borrowing for corporations whose investors rely on block size CDS.

Generally, economic studies have shown that block trades benefit from different market structures than non-block trades.[592] These studies suggest that pre-trade transparency can be particularly costly for block trades as prices are likely to move adversely if the existence of a large unexecuted order becomes known. Other traders may front run the block trade order or simply infer information about future price movements from its presence, thus potentially making it more costly for the block-initiating participant to find a counterparty willing to trade at an acceptable price. In addition, if a block trade interacts with other trading interest on a SB SEF, there might not be enough liquidity on the SB SEF to execute the entire block trade, leaving a portion of the block trade unexecuted, or requiring the block to be broken into smaller order sizes, which also could

[590] Proposed Rule 702(d) under Regulation MC would require the Board of a SB SEF to have at least a majority of independent directors. *See* Regulation MC Proposing Release, *supra* note 82.

[591] *See, e.g.,* Ananth Madhavan, *Market Microstructure: A Survey,* J. of Fin. Markets, Vol. 3 (2000).

[592] *See, e.g.,* Bessembinder Paper, *supra* note 159.

lead to increased transaction costs and a decreased willingness of market participants to participate in block trades.

The Commission recognizes these potential costs and believes that the proposal mitigates these costs, because it would allow SB SEFs flexibility in setting their market structure and trading rules concerning block trades. This should allow SB SEFs to create certain trading structures, *e.g.,* multi-dealer RFQ platforms, that cater to block trades and others that cater to non-blocks. Moreover, under the proposed interpretation of the definition of SB SEF, for a transaction on an RFQ platform, the person exercising investment discretion for the transaction, whether it is the participant itself or the participant's customer, could choose to send the RFQ to less than all participants. Under this proposed interpretation, market participants would have the choice to determine how broad or how narrow to disseminate their intent to trade blocks. The Commission further notes that, if overall trading costs decline, then the costs of breaking up a block into smaller parcels and spreading out those parcels by market participants seeking to execute a block transaction may not actually increase.[593]

According to industry sources consulted by Commission staff,[594] the monetary cost of forming a SB SEF is estimated to range from approximately $15 million to $20 million per SB SEF for the first year of operation, if an entity were to establish a SB SEF without the benefit of modifying an already existing trading system. The industry sources consulted by Commission staff estimate that, for the first year of operation, the cost of software and product development would range from approximately $6.5 million to $10.5 million per SB SEF. The technological costs would be expected to decline considerably during the second and subsequent years of operation, and are estimated to be in the range of $3 million to $4 million per year per SB SEF. For entities that currently own and/or operate platforms for the trading of OTC derivatives, the cost of forming a SB SEF would be more incremental, given that these entities already have viable technology that could be modified to comply with the requirements that the Commission may impose for SB SEFs. According to industry sources, the incremental costs of enhancing a trading platform to be compatible with any SB SEF requirements established by the Commission would range from as low as $50,000 to as much as $3 million per SB SEF, depending on the enhancements needed to establish a platform compatible with any Commission rules governing SB SEFs. The annual ongoing cost of maintaining the technology and any improvements is estimated to be in the range of $2 million to $4 million.[595]

In addition, the regulatory requirement of complying with the statutory Core Principles would increase the regulatory obligations of registered SB SEFs with respect to operating as a SB SEF and with respect to overseeing the participants that trade on their facilities. Industry sources estimate that the cost to an SB SEF of complying with the rules relating to surveillance and oversight they expected the Commission to propose would be in the range of $1 million to $3 million annually, with initial costs likely to be at the higher end of such range, since a SB SEF would need to create the technology necessary to monitor and surveil its market participants, as well as to create a rule book in compliance with the Core Principles and related rules. The ongoing annual compliance costs are estimated by industry sources to be approximately $1 million, which would include the salary of a CCO and at least two junior compliance personnel, expected to be attorneys.

The Commission requests comments on the accuracy of these estimates. Specifically, the Commission requests comment on how the Commission can most accurately estimate the cost and benefits of the proposed rules and interpretations. Are there any important benefits and costs not currently discussed? How would the costs and benefits differ between operators of current platforms or systems trading SB swaps? What are the potential costs and benefits of the pre-trade transparency requirement, block trade requirement, order interaction requirement and other market structure requirements included in the proposal?

We detail below cost estimates for specifics parts of the proposed rules. Many of these costs estimates are based on the PRA estimates of costs and burdens from Section XXVII, as well as other costs associated with the proposed rules.

Registration. The Commission preliminary estimates that the aggregate initial costs to all potential SB SEF registrants to file Form SB SEF, including all exhibits thereto, would be approximately $13,505,940,[596] or approximately $675,297 [597] per SB SEF.

The Commission estimates the initial costs (aside from the costs associated with Exhibits F, H and P, which are separately discussed below) associated with proposed Form SB SEF would be $32,000 per SB SEF, or $640,000 for all potential SB SEFs.[598] This would include the time required to compile the information required by proposed Form SB SEF, prepare the proposed Form SB SEF itself, and file it with the Commission. In addition, Exhibits F and H to proposed Form SB SEF would require an applicant to submit financial reports that would need to satisfy a number of requirements, including the requirement that a certified public account audit each financial report relating to the SB SEF and a requirement that unaudited financial information be provided for certain affiliated entities of the SB SEF.[599] The Commission preliminarily believes that it is unlikely that during the initial implementation period a potential registrant would have audited financial statements for the SB SEF in the ordinary course of business prior to applying for registration on Form SB SEF. Therefore, in order to register as a SB SEF with the Commission on Form SB SEF and comply with Exhibits F and H thereto, potential registrants would incur an initial cost to generate such financial statements. Based on conversations with operators of current

[593] *See, e.g.,* Amber Anand, *et al., Market Crashes and Institutional Trading,* Working Paper, Social Science Research Network (2010).

[594] In discussing estimated costs with Commission staff, these industry sources were generally familiar with the requirements of the Dodd-Frank Act and the Core Principles and related requirements specified therein, but were not aware of the specifics of the rules being proposed. Thus, they were able to provide the broad general estimates of projected costs, which are described here. More specific estimates as to the costs associated with specific rules are detailed further below.

[595] Although there currently are trading systems that trade SB swaps on an OTC basis, the Commission preliminarily believes that no such systems are currently in operation that would comply, without modifications, with the requirements of proposed Regulation SB SEF.

[596] *See infra* note 597.

[597] $13,505,940/20 potential SB SEF registrants = $675,297.

[598] The Commission preliminarily estimates, for purposes of its PRA, that the average initial burden imposed by proposed Form SB SEF (other than Exhibits F, H and P of Form SB SEF) for SB SEF registration would be 100 hours per SB SEF. *See supra* Section XXVII. Assuming an hourly cost of $320 for a compliance attorney to meet these requirements, the one-time estimated dollar cost to register as a SB SEF would be $32,000 (100 hours × $320), or $640,000 ($32,000 × 20 SB SEFs) in the aggregate. The hourly rate for the compliance attorney is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[599] *See supra* Section XXVII.D.1.

trading platforms and the Commission's experience with entities of similar size, the Commission preliminarily estimates that each potential SB SEF registrant would incur, on average, a cost of $99,000 to complete the financial statements,[600] and a cost of $500,000 for independent public accounting services. In the aggregate, these costs are estimated to be $1,980,000[601] and $10,000,000,[602] respectively.[603]

The Commission also estimates that it would cost approximately $7,920 per respondent to compile, review, and submit the financial reports for certain affiliated entities as required pursuant to Exhibit H to proposed Form SB SEF, or $158,400 in the aggregate.[604] All of the financial statements required by Exhibits F and H to proposed Form SB SEF would need to be provided in XBRL, as required in Rules 405(a)(1), (a)(3), (b), (c), (d) and (e) of Regulation S–T.[605] This would create an additional cost for potential SB SEF respondents. The Commission preliminarily estimates, based on its experience with other data tagging initiatives, that these requirements would add an additional cost on average of approximately $12,096[606] and $23,000 in outside software and other costs per respondent, or $241,920[607] and $460,000[608] in the aggregate, respectively. Thus, for complying with the financial statement requirements under Exhibits F and H to proposed Form SB SEF, the Commission estimates a total initial cost of approximately $642,016 per respondent[609] and $12,840,320 in the aggregate for all respondents.[610]

Exhibit P to proposed Form SB SEF would require SB SEFs controlled by other persons and non-resident SB SEFs to provide opinions of counsel as required by Rules 801(e) and (f), respectively. Therefore, in order to register as a SB SEF with the Commission on Form SB SEF, potential registrants that are controlled by other persons or that are non-resident persons would incur an initial cost to generate such opinions of counsel. As discussed above, the Commission preliminarily estimates that the average initial paperwork cost for each SB SEF controlled by another person and each non-resident SB SEF to provide the opinion of counsel required by Exhibit P would be one hour and $900 per SB SEF. As discussed above, the Commission preliminarily estimates that all 20 estimated applicants seeking to register as SB SEFs would be controlled by other persons and that one applicant seeking to register as a SB SEF will be a non-resident person. Therefore, in the aggregate, the costs to comply with Exhibit P are estimated to be $24,400 for all SB SEFs controlled by other persons[611] and $1,220 for all non-resident SB SEFs.[612]

Therefore, the Commission preliminarily estimates that the total one-time aggregate cost for all respondents to file the initial Form SB SEF, including all exhibits thereto, would be approximately $13,505,940.[613]

After the initial year in which a SB SEF would be registered, the Commission estimates that each registered SB SEF would submit 4 amendments to Form SB SEF on average and one annual update, at an annual cost of $48,000 per SB SEF, or $960,000 in the aggregate.[614] In addition, the Commission estimates that two SB SEFs controlled by another person would each submit one amendment to Exhibit P to Form SB SEF per year, at an annual aggregate cost of $2,440.[615] The Commission also estimates that one non-resident SB SEF would submit one amendment to Exhibit P to Form SB SEF per year, at an annual cost of $1,220.[616]

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[600] The Commission preliminarily estimates, for purposes of its PRA, that the average initial burden would be 500 hours per SB SEF. *See supra* Section XXVII. Assuming an hourly cost of $198 for a senior accountant to meet these requirements, the one-time estimated dollar cost to register as a SB SEF would be $99,000 (500 hours × $198), or $1,980,000 ($99,000 × 20 SB SEFs) in the aggregate. The hourly rate for the senior accountant is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[601] $1,980,000 = $99,000 × 20 SB SEFs.

[602] $10,000,000 = $500,000 × 20 SB SEFs.

[603] *See also* Section XXVII.D.1.

[604] The Commission preliminarily estimates, for purposes of its PRA, that the average initial burden to comply with the financial statement requirements of Exhibit H to proposed Form SB SEF would be 40 hours per SB SEF. *See supra* Section XXVII. Assuming an hourly cost of $198 for a senior accountant to meet these requirements, the one-time estimated dollar cost per SB SEF would be $7,920 (40 hours × $198), or $158,400 ($7,920 × 20 SB SEFs) in the aggregate. The hourly rate for the senior accountant is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[605] *See* 17 CFR 232.405.

[606] The Commission preliminarily estimates, for purposes of its PRA, that the average initial burden would be 54 hours per SB SEF. *See supra* Section XXVII. Assuming an hourly cost of $224 for a programmer analyst to meet these requirements, the initial estimated dollar cost would be $12,096 (54 hours × $224), or $241,920 ($12,096 × 20 SB SEFs) in the aggregate. The hourly rate for the programmer analyst is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[607] $241,920 = $12,096 × 20 SB SEFs.

[608] $460,000 = $23,000 × 20 SB SEFs.

[609] $99,000 + $500,000 + $7,920 + $12,096 + $23,000 = $642,016.

[610] $12,840,320 = $642,016 × 20 SB SEFs.

[611] The Commission estimates that a SB SEF that is controlled by another person will assign these responsibilities to a compliance attorney. Assuming an hourly cost of $320 for a compliance attorney to meet these requirements, the one-time estimated dollar cost for a SB SEF controlled by another person to comply with Exhibit P would be $1,220 ((1 hour × $320) + $900), or $24,400 ($1,220 × 20 SB SEFs controlled by other persons) in the aggregate. The hourly rate for the compliance attorney is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[612] The Commission estimates that a non-resident SB SEF will assign these responsibilities to a compliance attorney. Assuming an hourly cost of $320 for a compliance attorney to meet these requirements, the one-time estimated dollar cost for a non-resident SB SEF to comply with Exhibit P would be $1,220 ((1 hour × $320) + $900). This would also be the aggregate initial cost as the Commission has estimated that only one non-resident person would seek to register as a SB SEF. The hourly rate for the compliance attorney is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[613] $13,505,940 = $640,000 (costs other than Exhibits F, H and P to Form SB SEF) + $12,840,320 (costs relating to Exhibits F and H to Form SB SEF) + $24,400 (costs relating to Exhibit P to Form SB SEF for SB SEFs controlled by other persons) + $1,220 (costs relating to Exhibit P to Form SB SEF for all non-resident SB SEFs).

[614] The Commission preliminarily estimates, for purposes of its PRA, that the average annual burden to prepare and file rule amendments and the annual update to Form SB SEF would be 150 hours per SB SEF. *See supra* Section XXVII. Assuming an hourly cost of $320 for a compliance attorney to meet these requirements, the annual estimated dollar cost would be $48,000 (150 hours × $320), or $960,000 ($48,000 × 20 SB SEFs) in the aggregate. The hourly rate for the compliance attorney is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[615] The Commission estimates that a SB SEF that is controlled by another person will assign these responsibilities to a compliance attorney. Assuming an hourly cost of $320 for a compliance attorney to meet these requirements, the annual estimated dollar cost for a SB SEF controlled by another person to amend Exhibit P would be $1,220 ((1 hour × $320) + $900), or $2,440 in the aggregate ($1,220 × 2 (estimated number of SB SEFs controlled by other persons required to amend Exhibit P per year) × 1 amendment). The hourly rate for the compliance attorney is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[616] The Commission estimates that a non-resident SB SEF will assign these responsibilities to a compliance attorney. Assuming an hourly cost of $320 for a compliance attorney to meet these requirements, the annual estimated dollar cost for a non-resident SB SEF to amend Exhibit P would be $1,220 ((1 hour × $320) + $900). This would also be the aggregate annual cost as the Commission has

In addition, proposed Rule 804 would impose costs on SB SEFs seeking to withdraw registration. The Commission estimates that one SB SEF would seek to withdraw its registration per year. Therefore, the Commission estimates that the aggregate annual estimated dollar cost for SB SEFs seeking to withdraw registration would be $320.[617]

Finally, proposed Rule 803 would impose costs on SB SEFs to prepare and file supplemental information with the Commission. The Commission estimates that the average annual cost for a SB SEF to prepare and file such supplemental information would be $2,400 for each SB SEF, or $48,000 in the aggregate.[618]

Thus, the Commission estimates that the total annual aggregate cost of making all required filings related to Form SB SEF would be approximately $1,011,980.[619]

The Commission solicits comments on the costs associated with the registration related rules and new Form SB SEF and exhibits. The Commission specifically requests comment on initial costs associated with completing the registration form and ongoing annual costs of completing the required periodic and annual amendments. Please describe and, to the extent practicable, quantify the costs associated with any comments that are submitted. In addition, the Commission requests comment on the following:

- How can the Commission most accurately estimate the costs and benefits arising from proposed Regulation SB SEF's registration requirements?
- What are the costs currently borne by entities covered by the proposed registration requirements that may have been included in the Commission's analysis?
- Are there additional costs involved in complying with the registration requirements that have not been identified? If so, what are the types, and amounts, of such costs?
- Can commenters assess the benefits of having comprehensive and accurate registration of SB SEFs, which would provide access to such information to the Commission and other regulators?
- Would there be additional benefits from the proposed registration requirements that have not been identified?

Rules Generally. The Commission estimates that the initial cost for SB SEFs to comply with the rule writing requirements of Regulation SB SEF, including to establish and submit the rules to the Commission, would be $73,600 for each SB SEF, for an aggregate initial cost of $1,472,000.[620] The estimated cost would include the time expended for drafting the rules, and for review of the draft rules, policies or procedures by the SB SEF's senior management.

The Commission notes that a SB SEF may choose to refine the rules, policies or procedures that it would establish in connection with the requirements of Regulation SB SEF. Once a SB SEF has drafted the written rules, policies and procedures it is required to establish pursuant to Regulation SB SEF, the Commission estimates that it would cost a SB SEF approximately $38,400 annually to update its rules, for an aggregate estimated ongoing annual cost for all SB SEFs of approximately $768,000.[621]

The Commission requests comment on the costs and benefits of the proposed rule writing requirements discussed above, as well as any costs and benefits not already described that could result. The Commission also requests data to quantify any potential costs or benefits. The Commission requests comment on the costs and benefits of the proposed registration requirements discussed above, as well as any costs and benefits not already described that could result. The Commission also requests data to quantify any potential costs or benefits. In addition, the Commission requests comment on the following:

- How can the Commission most accurately estimate the costs and benefits arising from the proposed rule writing requirements of Regulation SB SEF?
- What are the costs currently borne by entities that may have been included in the Commission's analysis of the costs of the proposed rule writing requirements?
- Are there additional costs involved in complying with the rule writing requirements that have not been identified? If so, what are the types, and amounts, of such costs?
- Can commenters assess the benefits of having a comprehensive and accurate rule writing requirement for SB SEFs, which would provide access to such information to the Commission and other regulators?
- Would there be additional benefits from the proposed rule writing requirements that have not been identified?

Reporting. The Commission estimates that the annual cost for SB SEFs to comply with the reporting requirements of Regulation SB SEF would be $387,200 per SB SEF, for an aggregate annual cost of $7,744,000.[622] Further,

estimated that only one non-resident person would seek to register as a SB SEF, and that such non-resident SB SEF will only file one amendment to Exhibit P per year. The hourly rate for the compliance attorney is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[617] The Commission preliminarily estimates, for purposes of its PRA, that the average burden for a SB SEF to withdraw its registration would be 1 hour. *See supra* Section XXVII. Assuming an hourly cost of $320 for a compliance attorney to meet these requirements, the estimated dollar cost to withdraw the registration of a SB SEF would be $320 (1 hour × $320). This would also be the aggregate annual cost as the Commission has estimated that only one SB SEF would seek to withdraw its registration as a SB SEF per year. The hourly rate for the compliance attorney is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[618] The Commission preliminarily estimates, for purposes of its PRA, that the average annual burden to prepare and file supplemental information would be 7.5 hours per SB SEF. *See supra* Section XXVII. Assuming an hourly cost of $320 for a compliance attorney to meet these requirements, the estimated annual dollar cost would be $2,400 (7.5 hours × $320), or $48,000 ($2,400 × 20 SB SEFs) in the aggregate. The hourly rate for the compliance attorney is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[619] $1,011,980 = $960,000 + $2,440 + $1,220 + $320 + $48,000.

[620] The Commission preliminarily estimates, for purposes of its PRA, that the average initial burden to comply with the rule-writing requirements of Regulation SB SEF would be 230 hours per SB SEF. *See supra* Section XXVII. Assuming an hourly cost of $320 for a compliance attorney to meet these requirements, the initial estimated dollar cost would be $73,600 (230 hours × $320), or $1,472,000 ($73,600 × 20 SB SEFs) in the aggregate. The hourly rate for the compliance attorney is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[621] The Commission preliminarily estimates, for purposes of its PRA, that the average annual burden to comply with the rule-writing requirements of Regulation SB SEF would be 120 hours per SB SEF. *See supra* Section XXVII. Assuming an hourly cost of $320 for a compliance attorney to meet these requirements, the annual estimated dollar cost would be $38,400 (120 hours × $320), or $768,000 ($38,400 × 20 SB SEFs) in the aggregate. The hourly rate for the compliance attorney is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[622] The Commission preliminarily estimates, for purposes of its PRA, that the average annual costs comply with the reporting requirements of Regulation SB SEF would be 1,210 hours per SB SEF. *See supra* Section XXVII. Assuming an hourly cost of $320 for a compliance attorney to meet these

Continued

the Commission estimates the total cost of hiring outside legal counsel to review an international information sharing agreement to be $4,000 per SB SEF, for an aggregate cost of approximately $80,000 [623] for all SB SEFs. In addition, the Commission estimates the total annual cost of hiring an objective, external firm to review internal audits to be $90,000 per SB SEF, for an aggregate cost of approximately $1,800,000 [624] for all SB SEFs. Thus, the estimated aggregate total annual costs associated with reporting requirements for all SB SEFs would be approximately $9,624,000.[625]

The Commission estimates that the annual cost for SB SEF participants to comply with the reporting requirements of Regulation SB SEF would be $32,000 per SB SEF participant, for an aggregate annual cost of $8,800,000.[626]

The Commission requests comment on the costs and benefits of the proposed reporting requirements discussed above, as well as any costs and benefits not already described that could result. The Commission also requests data to quantify any potential costs or benefits. In addition, the Commission requests comment on the following:

- How can the Commission most accurately estimate the costs and benefits arising from proposed reporting requirements?
- What are the costs currently borne by entities that may have been included in the Commission's analysis of the costs of the proposed reporting requirements?
- Are there additional costs involved in complying with the reporting requirements that have not been identified? If so, what are the types, and amounts, of such costs?
- Can commenters assess the benefits of having comprehensive and accurate reporting requirements for SB SEFs, which would provide access to such information to the Commission and other regulators?
- Would there be additional benefits from the proposed reporting requirements that have not been identified?

Recordkeeping. The Commission estimates that the annual cost for SB SEFs to comply with the recordkeeping requirements of proposed Rule 818(a)–(b) would be similar to the annual cost for national securities exchanges to comply with comparable rules. The Commission estimates that the annual cost would be $16,000 per SB SEF, for an aggregate annual cost of $320,000.[627] This figure includes, but is not limited to, the annual hourly burden to generate, collect, organize and preserve all of the documents and other records required under proposed Rule 818(a) and (b).

In addition, proposed Rule 818(c) would require a SB SEF to keep certain records with respect to trading activity on and through the SB SEF. Specifically, a SB SEF must make and keep accurate, time-sequenced records of all inquiries, responses, orders, quotations, other trading interest and transactions that are received by, originated on, or executed on the SB SEF. The Commission estimates that the annual cost to comply with this requirement would be $41,600 per SB SEF, for an aggregate annual cost of $832,000.[628]

The Commission preliminarily estimates that a SB SEF could incur a one-time cost to set up or modify an existing recordkeeping system to comply with proposed Rule 818. Based on the Commission's experience with recordkeeping costs, and consistent with prior cost estimates for similar recordkeeping provisions,[629] the Commission estimates that setting up or modifying a recordkeeping system would cost $106,680 per SB SEF, for an aggregate total of $2,133,600.[630]

Additionally, the Commission preliminarily estimates that each SB SEF may have a one-time burden to upgrade its existing systems to ensure that the audit trail component of its systems complies with proposed Rule 818(c). Based on industry sources, the Commission preliminarily believes that this work would be done internally by two programmers over the course of approximately four weeks. The Commission preliminarily estimates that it would cost a total of $97,280 per SB SEF, or $1,945,600 in the aggregate for all SB SEFs.[631]

As discussed above, proposed Rule 809(d) would require a SB SEF that permits non-registered ECPs to be participants in the SB SEF to establish, document, and maintain a system of risk management controls and supervisory procedures reasonably designed to manage the financial, regulatory, and other risks of this business activity. Based on conversations with industry

requirements, the annual estimated dollar cost would be $387,200 (1,210 hours × $320), or $7,744,000 ($387,200 × 20 SB SEFs) in the aggregate. The hourly rate for the compliance attorney is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[623] $80,000 = $4,000 × 20 SB SEFs.

[624] $1,800,000 = $90,000 × 20 SB SEFs.

[625] $9,624,000 = $7,744,000 + $80,000 + $1,800,000.

[626] The Commission preliminarily estimates, for purposes of its PRA, that the average annual costs to comply with the reporting requirements of Regulation SB SEF would be 100 hours per SB SEF participant, with an estimated 275 SB SEF participants in total for a total of 27,500 hours. *See supra* Section XXVII. Assuming an hourly cost of $320 for a compliance attorney to meet these requirements, the annual estimated dollar cost would be $32,000 (100 hours × $320), or $8,800,000 ($32,000 × 275 SB SEF participants) in the aggregate. The hourly rate for the compliance attorney is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[627] The Commission preliminarily estimates, for purposes of its PRA, that the average annual burden to comply with the recordkeeping requirements of proposed Rule 818(a)–(b) would be 50 hours per SB SEF. *See supra* Section XXVII. Assuming an hourly cost of $320 for a compliance attorney to meet these requirements, the annual estimated dollar cost would be $16,000 (50 hours × $320), or $320,000 ($16,000 × 20 SB SEFs) in the aggregate. The hourly rate for the compliance attorney is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[628] The Commission preliminarily estimates, for purposes of its PRA, that the average annual burden to comply with the recordkeeping requirements of proposed Rule 818(c) would be 130 hours per SB SEF. *See supra* Section XXVII. Assuming an hourly cost of $320 for a compliance attorney to meet these requirements, the annual estimated dollar cost would be $41,600 (130 hours × $320), or $832,000 ($41,600 × 20 SB SEFs) in the aggregate. The hourly rate for the compliance attorney is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[629] *See* Securities Exchange Act Release No. 59342 (February 2, 2009); 74 FR 6456 (February 9, 2009) (Amendments to Rules for Nationally Recognized Statistical Rating Organizations) ("NRSRO Adopting Release").

[630] The Commission estimates it would take 345 hours for a senior programmer to set up or modify a recordkeeping system for a cost of $104,880 per SB SEF (345 hours × $304), or $2,097,600 ($104,880 × 20 SB SEFs). In addition, the Commission estimates a cost of $1,800 per SB SEF in information technology expenses to purchase recordkeeping software for a total initial cost of $36,000 for all SB SEFs. The total costs would be $106,680 ($104,880 + $1,800) per SB SEF or a total of $2,133,600 ($106,680 × 20 SB SEFs) for all SB SEFs. The hourly rate for the senior programmer is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[631] The Commission estimates that it would take 160 hours for two senior programmers to set up or modify a recordkeeping system for a cost of $97,280 per SB SEF (160 hours × 2 programmers × $304), or $1,945,600 ($97,280 × 20 SB SEFs) for all SB SEFs. The hourly rate for the senior programmer is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

sources, the Commission preliminarily believes that the majority of entities that would seek to become SB SEFs already would have risk management systems and supervisory procedures and controls to protect the integrity of their business and to comply with other requirements already specified and accounted for herein. The Commission also believes that only a small number of entities would have to establish completely new systems and procedures to comply with the requirement of proposed Rule 809(d).

The Commission estimates that each SB SEF would spend an average of $68,400 to modify its risk management systems to bring them into compliance with the proposed Rule for a total one-time cost of $1,368,000 for all SB SEFs combined,[632] and a total annual ongoing burden of $1,048,800 on all SB SEFs to maintain their systems.[633] The Commission preliminarily believes that proposed Rule 809(d) also would impose a one-time legal and compliance cost of $330,300 on all SB SEFs to comply with the requirement to establish, document, and maintain compliance policies and supervisory procedures,[634] and an annual cost of $482,700 on all SB SEFs to review their written compliance policies and supervisory procedures.[635]

Therefore, the Commission preliminarily estimates that the total one-time burden for all SB SEFs to comply with the collection of information requirements of proposed Rule 809(d) would be $1,698,300,[636] and the total annual burden for all SB SEFs to comply with the proposed Rule would be $1,531,500.[637]

The Commission requests comment on the costs and benefits of the proposed recordkeeping requirements discussed above, as well as any costs and benefits not already described that could result. The Commission also requests data to quantify any potential costs or benefits. In addition, the Commission requests comment on the following:

- How can the Commission most accurately estimate the costs and benefits arising from the proposed recordkeeping requirements?
- What are the costs currently borne by entities that may have been included in the Commission's analysis of the costs of the proposed recordkeeping requirements?
- Are there additional costs involved in complying with the recordkeeping requirements that have not been identified? If so, what are the types, and amounts, of such costs?
- Can commenters assess the benefits of having comprehensive and accurate recordkeeping requirements for SB SEFs, which would provide access to such information to the Commission and other regulators?
- Are the Commission's estimates concerning what it would cost to implement and maintain technology systems to comply with the recordkeeping requirements accurate? If not, what would the costs, in both time and dollar figures, be? Please provide data.
- Would there be additional benefits from the proposed recordkeeping requirements that have not been identified?

Publication of Trading Information. For the requirement in proposed Rule 817(a) that a SB SEF have the capacity to electronically capture, transmit, and disseminate information on price, trading volume, and other trading data on all SB swaps executed on or through the SB SEF, the Commission preliminarily estimates that a SB SEF would incur a one-time cost of $92,416 per SB SEF, or $1,848,320 in the aggregate.[638]

The Commission requests comment on the costs and benefits of the requirements discussed above, as well as any costs and benefits not already described that could result. The Commission also requests data to quantify any potential costs or benefits. In addition, the Commission requests comment on the following:

- How can the Commission most accurately estimate the costs and benefits arising from the proposed publication of trading information requirements?
- What are the costs currently borne by entities that may have been included in the Commission's analysis of the costs of the proposed publication of trading information requirements?
- Are there additional costs involved in complying with the publication of trading information requirements that have not been identified? If so, what are the types, and amounts, of such costs?
- Can commenters assess the benefits of having these requirements for SB SEFs, which would provide access to such information to the Commission and other regulators?

[632] The Commission preliminarily estimates, for purposes of its PRA, that the average one-time cost to comply with proposed Rule 809(d) would require one senior programmer working 225 hours. *See supra* Section XXVII. Assuming an hourly cost of $304 for a senior programmer the one-time cost would be $68,400 (225 hours × $304), or $1,368,000 ($68,400 × 20) in the aggregate. The hourly rate for the senior programmer is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[633] The Commission preliminarily estimates, for purposes of its PRA, that the ongoing cost to comply with proposed Rule 809(d) would require one senior programmer working 172.5 hours annually. *See supra* Section XXVII. Assuming an hourly cost of $304 for a senior programmer, the cost would be $52,440 (172.5 hours × $304), or $1,048,800 ($52,440 × 20 SB SEFs) in the aggregate. The hourly rate for the senior programmer is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[634] The Commission preliminarily estimates, for purposes of its PRA, that the average one-time cost to comply with proposed Rule 809(d) would require one compliance attorney and one compliance manager to spend 7.5 hours each to evaluate appropriate access thresholds. The Commission also preliminarily estimates that one compliance attorney and one compliance manager would each require approximately 15 hours, and the CCO would require approximately 7.5 hours, to set up or modify compliance policies and procedures to comply with the proposed rule. *See supra* Section XXVII. Assuming an hourly cost of $320 for a compliance attorney, $423 for the CCO, and $273 for a compliance manager the cost for each SB SEF would be $16,515 = 7,200 (22.5 hours × $320) + $3,172.5 (7.5 hours × $423) + $6,142.5 (22.5 hours × $273), for a total of $330,300 for all SB SEFs ($16,515 × 20). The hourly rate for the compliance attorney, compliance manager and CCO are from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[635] The Commission preliminarily estimates, for purposes of its PRA, that the ongoing cost to comply with proposed Rule 809(d) would require an average of 30 hours per year for each of an compliance attorney and compliance manager, and 15 hours per year for the CCO, to review and document their written compliance policies and supervisory procedures. Assuming an hourly cost of $320 for a compliance attorney, $423 for the CCO, and $273 for a compliance manager, the cost for each SB SEF would be 24,135 = $9,600 (30 hours × $320) + $6,345 (15 hours × $423) + $8,190 (30 hours × $273), for a total of $482,700 for all SB SEFs ($24,135 × 20 SB SEFs). The hourly rate for the compliance attorney, compliance manager and CCO are from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[636] $1,698,300 = $1,368,000 + $330,300. *See supra* notes 632 and 634 (discussing the average one-time costs to comply with Rule 809(d)).

[637] $1,531,500 = $1,048,800 + $482,700. *See supra* notes 633 and 635 (discussing the ongoing costs to comply with Rule 809(d)).

[638] The Commission preliminarily estimates, for purposes of its PRA, that the average one-time cost to comply with proposed Rule 817(a) would require two senior programmers working 160 hours, for a total of 320 hours. *See supra* Section XXVII. Assuming an hourly cost of $304 for a senior programmer, the one-time cost would be $92,416 (320 hours × $304), or $1,848,320 ($92,416 × 20 SB SEFs) in the aggregate. The hourly rate for the senior programmer and programmer analyst are from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

• Would there be additional benefits from the proposed publication of trading information requirements that have not been identified?

Composite Indicative Quote and Executable Bids and Offers. For the two requirements: (1) The requirement in proposed Rule 811(e) that a SB SEF operating a RFQ platform create and disseminate through the SB SEF a composite indicative quote, made available to all participants, for SB swaps traded on or through the SB SEF; and (2) the requirement imposed by the Commission's proposed interpretation of the definition of SB SEF that each SB SEF, at a minimum, provide any participant with the ability to make and display executable bids or offers accessible to all participants on the SB SEF, if the participant wishes to do so, the Commission preliminarily estimates that a SB SEF would incur a one-time cost of $21,120 per SB SEF, or $422,400 in the aggregate.[639] Further, the Commission preliminarily estimates that each SB SEF would incur a recurring annual cost of $11,200 to monitor and update its systems to determine if its composite indicative quote and executable bid and offer functionalities operate appropriately.[640]

The Commission requests comment on the costs and benefits of collecting and disseminating a composite indicative quote and of allowing participants to disseminate executable bids and offers discussed above, as well as any costs and benefits not already described that could result. The Commission also requests data to quantify any potential costs or benefits. In addition, the Commission requests comment on the following:

• How can the Commission most accurately estimate the costs and benefits arising from the proposed requirements to collect and disseminate a composite indicative quote and executable bids and offers?

• What are the costs currently borne by entities that may have been included in the Commission's analysis of the costs of the proposed dissemination of a composite indicative quote?

• Are there additional costs involved in complying with the requirements to collect and disseminate a composite indicative quote and providing the ability for participants to disseminate executable bids and offer that have not been identified? What are the types, and amounts, of the costs?

• Can commenters assess the benefits of collecting and disseminating a composite indicative quote for SB SEFs and of SB SEFs providing participants the ability to disseminate executable bids and offers?

Rule and Product Filings. The Commission estimates that the annual cost for SB SEFs to comply with the proposed rule and product filing requirements of proposed Rules 805 through 808 would be $75,200 per SB SEF, for an aggregate annual cost of $1,504,000.[641] These estimated costs entail preparing, reviewing and submitting the filings to the Commission. Based on the Commission staff's consultation with CFTC staff, the Commission believes that SB SEFs would handle the rule and product filing processes internally.

The Commission requests comment on the costs and benefits of the proposed rule and product filing requirements discussed above, as well as any costs and benefits not already described that could result. The Commission also requests data to quantify any potential costs or benefits. In addition, the Commission requests comment on the following:

• How can the Commission most accurately estimate the costs and benefits arising from the proposed rule and product filing requirements?

• What are the costs currently borne by entities that may have been included in the Commission's analysis of the costs of the proposed rule and product filing requirements?

• Are there additional costs involved in complying with the rule and product filing requirements that have not been identified? If so, what are the types, and amounts, of such costs?

• Can commenters assess the benefits of having comprehensive and accurate rules and product filing requirements for SB SEFs, which would provide access to such information to the Commission and other regulators?

• Would there be additional benefits from the proposed rule and product filing requirements that have not been identified?

Chief Compliance Officer. The Commission estimates that the initial cost for SB SEFs to comply with the CCO requirements of proposed Rule 823(b)(6) and (7), which relate to the handling of noncompliance issues, would be $91,200 per SB SEF, for an aggregate annual cost of $1,824,000.[642] A CCO also would be required under proposed Rule 823(c) and (d) to prepare and submit an annual compliance report to the Commission and to the SB SEF's Board. The Commission estimates that the annual cost for SB SEFs to comply with this requirement is $29,440 per SB SEF, for an aggregate annual cost of $588,800.[643] Proposed Rule 823(e)(1)

[639] The Commission preliminarily estimates, for purposes of its PRA, that the average one-time cost to comply with the above requirements would require one senior programmer and one programmer analyst working 40 hours each. *See supra* Section XXVII. Assuming an hourly cost of $304 for a senior programmer and $224 for a programmer analyst, the one-time cost would be $21,120 ((40 hours × $304) + (40 hours × $224)), or $422,400 ($21,120 × 20 SB SEFs) in the aggregate. The hourly rate for the senior programmer and programmer analyst are from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[640] The Commission preliminarily estimates, for purposes of its PRA, that the average annual cost to comply with the above requirements would require one programmer analyst working 50 hours. *See supra* Section XXVII. Assuming an hourly cost of $224 for a programmer analyst the one-time cost would be $11,200 (50 hours × $224), or $224,000 ($11,200 × 20 SB SEFs) in the aggregate. The hourly rate for the senior programmer and programmer analyst are from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[641] Based on the Commission staff's consultation with CFTC staff, the Commission preliminarily estimates for purposes of its PRA that the average annual burden to comply with the rule filing requirements of Rules 805 and 806 would be 150 hours, and the average annual burden to comply with the product filing requirements of Rules 807 and 808 would be 85 hours per SB SEF. *See supra* Section XXVII. Assuming an hourly cost of $320 for a compliance attorney to meet these requirements, the annual estimated dollar cost would be $75,200 (235 hours × $320), or $1,504,000 ($75,200 × 20 SB SEFs) in the aggregate. The hourly rate for the compliance attorney is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[642] The Commission preliminarily estimates, for purposes of its PRA, that the average initial burden to comply with the CCO requirements of proposed Rule 823(b)(6) and (7) would be 160 hours. Also, due to the novel nature of the CCO requirements in the SB SEF industry and the new requirements under the Dodd-Frank Act, the Commission estimates that there would be an initial one-time burden of $40,000 per SB SEF in outside legal costs. *See supra* Section XXVII. Assuming an hourly cost of $320 for a compliance attorney to meet these requirements, the annual estimated dollar cost would be $51,200 (160 hours × $320) plus $40,000, for a total of $91,200, or $1,824,000 ($91,200 × 20 SB SEFs) in the aggregate. The hourly rate for the compliance attorney is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[643] The Commission preliminarily estimates, for purposes of its PRA, that the average initial burden to comply with the CCO requirements of proposed Rule 823(c) and (d) would be 92 hours. *See supra* Section XXVII. Assuming an hourly cost of $320 for a compliance attorney to meet these requirements, the annual estimated dollar cost would be $29,440 (92 hours × $320) or $588,800 ($29,440 × 20 SB SEFs) in the aggregate. The hourly rate for the compliance attorney is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to

and (2) and Exhibits F and H to proposed Form SB SEF also require the CCO to submit an annual financial report. Based on conversations with operators of current trading platforms and the Commission's experience with entities of similar size, the Commission preliminarily estimates that each SB SEF would incur, on average, a cost of $99,500 to complete the reports,[644] and a cost of $500,000 for independent public accounting services. In the aggregate, these costs are estimated to be $1,980,000 and $10,000,000, respectively.[645] The Commission also estimates that it would cost approximately $7,920 per respondent to compile, review, and submit the financial reports for certain affiliated entities or $158,400 in the aggregate.[646] However, all of these reports would need to be provided in XBRL, as required by Rules 405(a)(1), (a)(3), (b), (c), (d) and (e) of Regulation S–T.[647] This would create an additional cost for SB SEFs. The Commission preliminarily estimates, based on its experience with other data tagging initiatives, that these requirements would add an additional cost on average of approximately $12,096[648] and $23,000 in outside software and other costs per respondent, or $241,920 and $460,000 in the aggregate, respectively. Thus, the Commission estimates a total initial cost of approximately $762,656 per respondent[649] and $15,253,120 in the aggregate for all respondents.[650]

The Commission requests comment on the costs and benefits of the proposed CCO requirements discussed above, as well as any costs and benefits not already described that could result. The Commission also requests data to quantify any potential costs or benefits. In addition, the Commission requests comment on the following:

- How can the Commission most accurately estimate the costs and benefits arising from the proposed CCO requirements?
- What are the costs currently borne by entities that may have been included in the Commission's analysis of the cost of the proposed CCO requirements?
- Are there additional costs involved in complying with the CCO requirements that have not been identified? If so, what are the types, and amounts, of such costs?
- Can commenters assess the benefits of having comprehensive and accurate CCO requirements for SB SEFs, which would provide access to such information to the Commission and other regulators?
- Would there be additional benefits from the proposed CCO requirements that have not been identified?

Conflicts of Interest. As described above, proposed Rule 820 sets forth certain governance arrangements that would be required of SB SEFs. A SB SEF may need to revise the composition of its Board, if the Board currently is not composed of at least 20% SB SEF participants. A SB SEF could comply with the 20% participant director requirement by decreasing the size of its Board and allowing some non-participant directors to resign, maintaining the current size of its Board and replacing some non-participant directors with participant directors, or by increasing the size of its Board and electing additional participant directors. In any event, unless a SB SEF currently complies with proposed Rule 820, it would incur the cost of adding new directors or replacing existing directors. A SB SEF may also need to design or modify its governance processes to preclude any participant, either alone or together with its related persons, that beneficially owns an interest in the SB SEF from dominating or exercising disproportionate influence in the selection of participant directors, if such participant could thereby dominate or exercise disproportionate influence in the selection or appointment of the entire Board. The Commission estimates a cost per SB SEF of $4,800, or $96,000 in the aggregate for all SB SEFs to revise the relevant governing documents.[651]

A SB SEF may also need to revise the composition of its Board to include at least one director that is representative of investors who are not SB swap dealers or major SB swap participants, and are not associated with a participant. In this regard, SB SEFs could face difficulties in locating qualified individuals to serve as investor directors, particularly because SB swaps trading is complex and some potential candidates may decline to serve as a director if they believe that they lack sufficient expertise. There could also be costs in educating investor directors to become familiar with the manner in which SB swaps are traded and the overall market for SB swaps, as well as the new regulatory structure that would govern them, which could slow Board or committee processes at least initially.

The Commission preliminarily believes that the cost of securing an investor director to serve on the Board of the SB SEF could range from a relatively low cost for those entities that have the contacts and resources to be able to search for one or more investor directors on their own; to a moderate cost for those entities that can undertake the search on their own but would incur some expenditures, such as placing advertisements in national media; to a higher cost for those entities that must secure the services of a recruitment firm that specializes in the placement of outside directors. The Commission preliminarily estimates that those SB SEFs that must rely on a recruitment specialist could incur a cost of approximately $68,000 per director,[652]

account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[644] The Commission preliminarily estimates, for purposes of its PRA, that the average initial burden would be 500 hours per SB SEF. *See supra* Section XXVII. Assuming an hourly cost of $198 for a senior accountant to meet these requirements, the one-time estimated dollar cost to register a SB SEF would be $99,000 (500 hours × $198), or $1,980,000 ($99,000 × 20 SB SEFs) in the aggregate. The hourly rate for the senior accountant is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[645] *Id. See also* Section XXVII.D.1.

[646] The Commission preliminarily estimates, for purposes of its PRA, that the average initial burden would be 40 hours per SB SEF. *See* supra Section XXVII. Assuming an hourly cost of $198 for a senior accountant to meet these requirements, the one-time estimated dollar cost per SB SEF would be $7,920 (40 hours × $198), or $158,400 ($7,920 × 20 SB SEFs) in the aggregate. The hourly rate for the senior accountant is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[647] *See* 17 CFR 232.405.

[648] The Commission preliminarily estimates, for purposes of its PRA, that the average initial burden would be 54 hours per SB SEF. *See supra* Section XXVII. Assuming an hourly cost of $224 for a programmer analyst to meet these requirements, the initial estimated dollar cost would be $12,096 (54 hours × $224), or $241,920 ($12,096 × 20 SB SEFs) in the aggregate. The hourly rate for the programmer analyst is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[649] $762,656 = $91,200 + $29,440 + $99,000 + $500,000 + $7,920 + $12,096 + $23,000.

[650] $15,253,120 = 20 (number of SB SEFs) × $762,656.

[651] The Commission preliminarily estimates, for purposes of its PRA, that it would take a compliance attorney approximately 15 hours to revise the relevant governing documents. Assuming an hourly cost of $320 for a compliance attorney to meet these requirements, the one-time estimated dollar cost would be $4,800 (15 hours × $320) or $96,000 ($4,800 × 20 SB SEFs) in the aggregate. The hourly rate for the senior programmer and programmer analyst are from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[652] The Commission is basing this estimate on a recent study noting that the retainer fee for outside

Continued

or $1,360,000 in the aggregate, if all SB SEFs utilized a recruitment firm.[653]

The Commission requests comment on the costs and benefits of the proposed conflicts requirements discussed above, as well as any costs and benefits not already described that could result. The Commission also requests data to quantify any potential costs or benefits. In addition, the Commission requests comment on the following:

- How can the Commission most accurately estimate the costs and benefits arising from the proposed conflicts requirements?
- What are the costs currently borne by entities that may have been included in the Commission's analysis of the costs of the proposed conflicts requirements?
- Are there additional costs involved in complying with the governance requirements that have not been identified? If so, what are the types, and amounts, of such costs?
- Can commenters assess the benefits of having governance requirements for SB SEFs?
- Would there be additional benefits from the proposed conflicts requirements that have not been identified?

Surveillance. The Commission preliminarily estimates that establishing an automated surveillance system in compliance with proposed Rules 811 and 813 would require an initial cost of $3,256,800 per SB SEF, or $65,136,000 in the aggregate. The initial cost per SB SEF includes $1,756,800 in initial programming costs per SB SEF[654] as well as a one-time capital expenditure per SB SEF of $1.5 million in information technology costs that would be necessary to establish such a system. This capital expenditure estimate is based on the Commission's discussions with market participants currently operating platforms that trade OTC swaps.

The Commission preliminarily estimates that the ongoing annual costs associated with the automated surveillance system required by proposed Rules 811 and 813 would be $1,306,400 per SB SEF, or $26,128,000 in the aggregate. The annual cost per SB SEF includes $806,400 in annual programming costs per SB SEF[655] as well as an ongoing annual information technology cost of $500,000 per SB SEF.

The Commission requests comment on the costs and benefits of the proposed surveillance system requirements discussed above, as well as any costs and benefits not already described that could result. The Commission also requests data to quantify any potential costs or benefits. In addition, the Commission requests comment on the following:

- How can the Commission most accurately estimate the costs and benefits arising from the proposed surveillance system requirements?
- What are the costs currently borne by entities that may have been included in the Commission's analysis of the costs of the proposed surveillance system requirements?
- Are there additional costs involved in complying with the surveillance system requirements that have not been identified? If so, what are the types, and amounts, of such costs?
- Can commenters assess the benefits of having comprehensive and accurate surveillance system requirements for SB SEFs, which would provide access to such information to the Commission and other regulators?
- Would there be additional benefits from the proposed surveillance system requirements that have not been identified?

D. General Request for Comments on Regulation SB SEF

- The Commission requests comment on any other aspect of the costs and benefits associated with Regulation SB SEF.
- Would the obligations imposed on reporting parties by proposed Regulation SB SEF be a significant enough barrier to entry to cause some firms not to enter the SB swaps market? If so, how many firms might decline to enter the market? How can the cost of their not entering the market be tabulated? How should the Commission weigh such costs, if any, against the anticipated benefits from increased transparency to the SB swaps market from the proposal, as discussed above?
- How many entities would be affected by proposed Regulation SB SEF?

XXIX. Consideration of Burden on Competition, and Promotion of Efficiency, Competition and Capital Formation

Section 3(f) of the Exchange Act[656] requires the Commission, whenever it engages in rulemaking and is required to consider or determine whether an action is necessary or appropriate in the public interest, to consider, in addition to the protection of investors, whether the action would promote efficiency, competition, and capital formation. In addition, Section 23(a)(2) of the Exchange Act[657] requires the Commission, when adopting rules under the Exchange Act, to consider the impact of any such rules on competition. Section 23(a)(2) of the Exchange Act also prohibits the Commission from adopting any rule that would impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.[658]

The Commission preliminarily believes that the regulation of SB SEFs, as required by the Dodd-Frank Act and proposed to be implemented under Regulation SB SEF, would promote efficiency, competition, and capital formation.

Promotion of Efficiency. The Commission preliminarily believes that the regulation of SB SEFs, as required by the Dodd-Frank Act and proposed to be implemented under Regulation SB SEF, would promote efficiency by encouraging innovation, automation, and reduction of informational asymmetries.

directors is on average $67,624 (rounded to $68,000). *See http://www.hewittassociates.com/_MetaBasicCMAssetCache_/Assets/Articles/2010/2010_Outside_Director_Compensation.pdf.* The Commission believes that this amount could serve as a proxy for the amount of any fee to be charged by a recruitment firm that would conduct a national search for a director that meets the requirements of proposed Rule 820(c)(2).

[653] $1,360,000 = 20 (number of SB SEFs) × $68,000.

[654] The Commission preliminarily estimates, for purposes of its PRA, that establishing an automated surveillance system would require one senior programmer and three additional programmers working for 1,800 hours each to create and implement such a system. *See supra* Section XXVII. Assuming an hourly cost of $304 for a senior programmer and $224 for a programmer analyst to meet these requirements, the initial estimated dollar cost would be $1,756,800 = (1,800 hours × $304) + ((1,800 hours × $224) × 3), or $35,136,000 ($1,756,800 × 20 SB SEFs) in the aggregate. The hourly rate for the senior programmer and programmer analyst are from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[655] The Commission preliminarily estimates, for purposes of its PRA, that the average annual burden to comply with the automated surveillance system requirements of proposed Rules 811 and 813 would require two programmer analysts working for 1,800 hours per SB SEF. *See supra* Section XXVII. Assuming an hourly cost of $224 for a programmer analyst to meet these requirements, the initial estimated dollar cost would be $806,400 (1,800 hours × $224 × 2), or $16,128,000 ($806,400 × 20 SB SEFs) in the aggregate. The hourly rate for the programmer analyst is from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[656] 15 U.S.C. 78c(f).

[657] 15 U.S.C. 78w(a)(2).

[658] *Id.*

The proposed rules are designed to be flexible and to foster innovation in the SB swaps market, particularly with respect to the trading of SB swaps by a diverse group of market participants. The Commission formulated the proposed rules, along with the proposed interpretation of the definition of SB SEF in a manner that would allow entities that seek to become SB SEFs to structure diverse platforms for the trading of SB swaps, subject to certain baseline requirements. These proposed baseline requirements are meant to permit access by a wide group of market participants to a range of SB swaps in keeping with the mandate of the Dodd-Frank Act. Thus, the Commission believes that the trading of SB swaps could evolve to its most efficient structure while also meeting the statutory and regulatory requirements relating to such activity.

The Commission preliminarily believes that the proposed requirements with respect to pre-trade price transparency could lead to more efficient pricing in the SB swaps market. The proposed rules are designed to result in an increase in pre-trade price transparency for SB swaps, which should aid market participants in evaluating current market prices for SB swaps, thereby furthering more efficient price discovery. Price transparency, coupled with the potential increase in the number of market participants with access to trading in SB swaps, could further decrease the spread in quoted prices, and thus could lead to higher efficiency in the trading of these securities.

Some industry participants, however, have expressed concerns to the Commission that pre-trade price transparency could force market participants to reveal more information about trading interest than they believe would be economically desirable. To the extent that market participants consider that pre-trade price transparency requirements are too burdensome and choose not to participate in the market, thereby foregoing any potential economic benefits that may have resulted from purchasing a particular SB swap, market efficiency could be harmed for less liquid instruments and for large blocks of SB swaps.

The Commission preliminarily believes that automation and systems development that would be associated with the regulation of SB SEFs, as required by proposed Regulation SB SEF, would provide market participants with new platforms and tools to execute and process transactions in SB swaps, which could result in lower trading costs and thus could lead to more efficient trading of SB swaps.

The Commission also believes that the proposed exemptions for SB SEFs from regulation as national securities exchanges or as brokers would eliminate what would be largely an additive oversight of SB SEFs and therefore would promote efficiency, because SB SEFs would not have to expend resources to comply with these regulatory obligations from which they would be exempt.

Promotion of Competition. The Commission preliminary believes that the regulation of SB SEFs, as required by the Dodd-Frank Act and proposed to be implemented under Regulation SB SEF, could promote competition. The proposed rules that would require SB SEFs to establish fair, objective and not unreasonably discriminatory standards for granting impartial access to trading on the SB SEF would foster greater access to SB SEFs by SB swap dealers, major SB swap participants, brokers, and ECPs. The resulting increase in the number of participants who could access venues for the trading of SB swaps would allow a range of market participants to compete for business on the SB SEF through price competition or other dimensions of service. The proposed pre-trade transparency requirements, including the proposed requirement to create and disseminate a composite indicative quote, could further promote price competition by making available information about trading interest before execution of the trade, thereby allowing participants to improve upon current quotes.

The Dodd-Frank Act's mandate to bring SB swaps that are subject to the mandatory clearing requirement and that are made available to trade onto regulated markets as well as the proposed interpretation of the definition of SB SEF, and proposed Regulation SB SEF that are intended to further implement the statutory directive, should help foster greater competition in the trading of SB swaps. The trading of SB swaps on regulated markets, and the Commission's proposals to institute rules for such trading, should allow diverse trading platforms or systems to register as SB SEFs and to compete for business in the SB swap market.

The Commission proposes to initially permit temporary registration of SB SEFs while it considers each applicant's full registration application, as long as the applicant meets certain requirements for temporary registration. This proposed temporary registration should help alleviate burdens associated with starting up a SB SEF and promote competition by reducing barriers to entry, because entry into the SB swap market would not be delayed by procedural matters, such as the timing of Commission review of the applicant's full registration submission. In addition, the Commission would have the opportunity to observe the SB SEF in operation before it grants permanent registration to the SB SEF, thereby helping to ensure that the SB SEF promotes desirable competition.

Promotion of Capital Formation. The Commission preliminary believes that the regulation of SB SEFs, as required by the Dodd-Frank Act and as proposed to be implemented under Regulation SB SEF, would promote capital formation because the proposed interpretation of the definition of SB SEF, along with the elements of proposed Rule 811 that relate to pre-trade price transparency, are intended to provide a flexible approach as to the parameters of what can be traded on a SB SEF. As a result, entities that currently provide a platform or system for OTC derivatives trading should be able to leverage off of their current trading platforms when developing a SB SEF-compatible trading platform. These entities would have various options available to them when developing their systems or platforms to comply with the Commission's proposed rulemaking. This flexible feature of the proposals should help promote capital formation because resources would be invested in a more efficient manner to improve upon or expand the features of those that plan to register as a SB SEF.

In addition, proposed Regulation SB SEF would provide the Commission with information relating to trading, recordkeeping, and surveillance of SB SEFs, as well as access to the books and records of SB SEFs. A well-regulated SB swap market, where the Commission has access to information about SB swap transactions, would increase the Commission's ability to assess risks in the SB swap market. In addition, the proposals would provide for various safeguards to help promote market integrity, including proposed Rule 809 relating to access to the SB SEF and proposed Rule 822 relating to systems safeguards. Proposed Regulation SB SEF also is intended to support the statutorily-mandated regulatory obligations of SB SEFs through proposed Rule 823 relating to the duties of the CCO, among other proposed rules. Any resulting increase in market integrity would likely increase market participants' confidence in the soundness and fairness of the SB swap market. Such increased confidence likely would stimulate financial investment in SB swaps by corporate

entities and others that may find that more transparent venues for the trading of SB swaps would allow them to purchase SB swaps to offset business risks and to meet hedging objectives. Further, to the extent that market participants utilize SB swaps to better manage portfolio risks with respect to positions in underlying securities, the extent that they are willing to participate in the SB swap market may impact their willingness to participate in the underlying asset's market. Therefore, the Commission preliminarily believes that the proposed rules would help encourage capital formation.

Burden on Competition. Based on discussions with industry participants, the Commission preliminarily believes that the start-up costs to become a SB SEF for those entities that currently own and/or operate a platform for the trading of OTC swaps would be moderate. According to these industry participants, any needed modifications to their systems or operations as a result of the Commission's proposals generally would entail the expenditure of resources chiefly on regulatory and compliance matters and on enhancing electronic systems to support both the operational and regulatory aspects of a SB SEF. A trading platform that currently trades OTC swaps would need to make some adjustments to its systems and structure to trade SB swaps in compliance with proposed Regulation SB SEF. The Commission preliminarily believes that the development and registration of, and introduction of trading in SB swaps by, a SB SEF would result in some barriers to entry that otherwise would not exist. This is particularly the case because, prior to the enactment of the Dodd-Frank Act, there were no statutory provisions mandating the trading of certain SB swaps on regulated markets.

The Commission requests comment on all aspects of this analysis and, in particular, on whether proposed Regulation SB SEF and the proposed interpretation of the definition of SB SEF would place a burden on competition, as well as the effect of the proposals on efficiency, competition, and capital formation. Commenters are requested to provide empirical data and other factual support for their views, if possible.

XXX. Consideration of Impact on the Economy

For purposes of the Small Business Regulatory Enforcement Fairness Act of 1996, or "SBREFA," the Commission must advise the OMB as to whether proposed Regulation SB SEF constitutes a "major" rule. Under SBREFA, a rule is considered "major" where, if adopted, it results or is likely to result in: (1) An annual effect on the economy of $100 million or more (either in the form of an increase or a decrease); (2) a major increase in costs or prices for consumers or individual industries; or (3) a significant adverse effect on competition, investment or innovation. If a rule is "major," its effectiveness will generally be delayed for 60 days pending Congressional review.

The Commission requests comment on the potential impact of proposed Regulation SB SEF on the economy on an annual basis, on the 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.

XXXI. Regulatory Flexibility Act Certification

The Regulatory Flexibility Act ("RFA") [659] requires Federal agencies, in promulgating rules, to consider the impact of those rules on small entities. Section 603(a) [660] of the Administrative Procedure Act,[661] as amended by the RFA, generally requires the Commission to undertake a regulatory flexibility analysis of all proposed rules, or proposed rule amendments, to determine the impact of such rulemaking on "small entities." [662] Section 605(b) of the RFA states that this requirement shall not apply to any proposed rule or proposed rule amendment, which if adopted, would not have a significant economic impact on a substantial number of small entities.[663]

A. Security-Based Swap Execution Facilities

The proposed rules and form under Regulation SB SEF would apply to all entities that seek to register with the Commission as a SB SEF and thus to operate as a SB SEF in compliance with Regulation SB SEF. In the Dodd-Frank Act, Congress defined for the first time the scope of a SB SEF and mandated the registration of these new entities. Based on its understanding of the market and conversations with industry sources, the Commission preliminarily believes that approximately 20 SB SEFs could be subject to the requirements of proposed Regulation SB SEF.

For purposes of Commission rulemaking in connection with the RFA, a small entity includes: (1i) 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,[664] 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,[665] 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.[666] Under the standards adopted by the Small Business Administration ("SBA"), entities in financial investments and related activities [667] are considered small entities if they have $7 million or less in annual receipts.

Based on the Commission's existing information about the SB swap market and the entities likely to register as SB SEFs, the Commission preliminarily believes that the entities likely to register as SB SEFs would not be considered small entities. The Commission preliminarily believes that most, if not all, of the SB SEFs would be large business entities or subsidiaries of large business entities, and that all SB SEFs would have assets in excess of $5 million and annual receipts in excess of $7,000,000. Therefore, the Commission preliminarily believes that none of the potential SB SEFs would be considered small entities.

[659] 5 U.S.C. 601 *et seq.*

[660] 5 U.S.C. 603(a).

[661] 5 U.S.C. 551 *et seq.*

[662] 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, 17 CFR 240.0–10. *See* Securities Exchange Act Release No. 18451 (January 28, 1982), 47 FR 5215 (February 4, 1982) (File No. AS–305).

[663] *See* 5 U.S.C. 605(b).

[664] *See* 17 CFR 240.0–10(a).

[665] *See* 17 CFR 240.17a–5(d).

[666] *See* 17 CFR 240.0–10(c).

[667] These entities would include firms involved in investment banking and securities dealing, securities brokerage, commodity contracts dealing, commodity contracts brokerage, securities and commodity exchanges, miscellaneous intermediation, portfolio management, providing investment advice, trust, fiduciary and custody activities, and miscellaneous financial investment activities. *See* SBA's Table of Small Business Size Standards, Subsector 523.

B. SB SEF Participants

The proposed rules under Regulation SB SEF also would impose requirements on participants of SB SEFs, *i.e.,* SB swap dealers, major SB swap participants, brokers and non-registered ECPs. Among other requirements relating to participants, SB SEFs would be required to establish and enforce rules that require its participants to maintain books and records of any trading interest, transaction, or position in any SB swap pertinent to their activity on the SB SEF and to provide prompt access to those books and records to the SB SEF and to the Commission. Based on conversations with industry sources, the Commission preliminarily believes that there could be a total of 275 persons that could become SB SEF participants and thus would thus be subject to the requirements of the proposed rules.[668]

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,[669] 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,[670] 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.[671] Under the standards adopted by the SBA, small entities in the finance and insurance industry include the following: (1) For entities in credit intermediation and related activities,[672] entities with $175 million or less in assets or, (2) for non-depository credit intermediation and certain other activities,[673] $7 million or less in annual receipts; (3) for entities in financial investments and related activities,[674] entities with $7 million or less in annual receipts; (4) for insurance carriers and entities in related activities,[675] entities with $7 million or less in annual receipts; and (5) for funds, trusts, and other financial vehicles,[676] entities with $7 million or less in annual receipts.

Based on feedback from industry participants about the SB swap market, the Commission preliminarily believes that the entities that will be participants of SB SEFs, whether SB swap dealers, major SB swap participants, registered brokers or non-registered ECPs, would exceed the thresholds defining "small entities" set out above. Thus, the Commission believes it is unlikely that proposed Regulation SB SEF, as it would affect SB SEF participants, would have a significant economic impact on any small entity.

C. Certification

For the foregoing reasons, the Commission certifies that the proposed rules and form under Regulation SB SEF would not have a significant economic impact on a substantial number of small entities for purposes of the RFA. The Commission requests comments regarding this certification. The Commission requests that commenters describe the nature of any impact on small entities and provide empirical data to illustrate the extent of the impact.

XXXII. Statutory Authority and Text of Proposed Amendments

Pursuant to the Exchange Act, 15 U.S.C. 78a *et seq.,* and particularly, Sections 3, 6, 15, 19, 23(a), 30(b), 30(c) and 36 (15 U.S.C. 78c, 78f, 78o, 78s, 78w(a), 78dd(b), 78dd(c) and 78mm), thereof, and Section 763 of the Dodd-Frank Act (15 U.S.C. 78c–4), the Commission is proposing to adopt § 240.15a–12, Regulation SB SEF and Form SB SEF under the Exchange Act and to amend § 240.3a1–1 under the Exchange Act.

List of Subjects in 17 CFR Parts 240, 242 and 249

Securities, brokers, reporting and recordkeeping requirements.

For the reasons stated in the preamble, the Commission 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 is revised and the following citation 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, 78d, 78e, 78f, 78g, 78i, 78j, 78j–1, 78k, 78k–1, 78l, 78m, 78n, 78n–1, 78o, 78o–4, 78p, 78q, 78s, 78u–5, 78w, 78x, 78ll, 78mm, 80a–20, 80a–23, 80a–29, 80a–37, 80b–3, 80b–4, 80b–11, and 7201 *et seq;* 18 U.S.C. 1350 and 12 U.S.C. 5221(e)(3), unless otherwise noted.

* * * * *

§ 240.15a–12 also issued under 15 U.S.C. 78c–4.

* * * * *

2. Section 240.3a1–1 is amended by adding paragraph (a)(4) and revising paragraph (b) introductory text to read as follows:

§ 240.3a1–1 Exemption from the definition of "Exchange" under Section 3(a)(1) of the Act.

(a) * * *

(4) Is a security-based swap execution facility, as that term is defined in section 3(a)(77) of the Act (15 U.S.C. 78c(a)(77)), that:

(i) Is in compliance with Regulation SB SEF (17 CFR 242.800 through 242.823); and

(ii) Does not serve as a marketplace for transactions in securities other than security-based swaps.

(b) Notwithstanding paragraph (a)(1), (a)(2), or (a)(3) of this section, an organization, association, or group of persons shall not be exempt under this section from the definition of "exchange," if:

* * * * *

3. Add § 240.15a–12 to read as follows:

[668] *See supra* Section XXVII.C.

[669] *See* 17 CFR 240.0–10(a).

[670] *See* 17 CFR 240.17a–5(d).

[671] *See* 17 CFR 240.0–10(c).

[672] This includes commercial banks, savings institutions, credit unions, firms involved in other depository credit intermediation, credit card issuing, sales financing, consumer lending, real estate credit, and international trade financing. *See* SBA's Table of Small Business Size Standards, Subsector 522.

[673] This includes firms involved in secondary market financing, all other non-depository credit intermediation, mortgage and nonmortgage loan brokers, financial transactions processing, reserve, and clearing house activities, and other activities related to credit intermediation. *See* SBA's Table of Small Business Size Standards, Subsector 522.

[674] This includes firms involved in investment banking and securities dealing, securities brokerage, commodity contracts dealing, commodity contracts brokerage, securities and commodity exchanges, miscellaneous intermediation, portfolio management, providing investment advice, trust, fiduciary and custody activities, and miscellaneous financial investment activities. *See* SBA's Table of Small Business Size Standards, Subsector 523.

[675] This includes direct life insurance carriers, direct health and medical insurance carriers, direct property and casualty insurance carriers, direct title insurance carriers, other direct insurance (except life, health and medical) carriers, reinsurance carriers, insurance agencies and brokerages, claims adjusting, third party administration of insurance and pension funds, and all other insurance related activities. *See* SBA's Table of Small Business Size Standards, Subsector 524.

[676] This includes pension funds, health and welfare funds, other insurance funds, open-end investment funds, trusts, estates, and agency accounts, real estate investment trusts and other financial vehicles. *See* SBA's Table of Small Business Size Standards, Subsector 525.

§ 240.15a–12 Conditional exemption from the regulation of brokers registered as security-based swap execution facilities.

(a) A security-based swap execution facility (as that term is defined in section 3(a)(77) of the Act (15 U.S.C. 78c(a)(77))) may register as a broker under section 15(a)(1) and (b) of the Act (15 U.S.C. 78o(a)(1) and (b)) by registering as a security-based swap execution facility, if such security-based swap execution facility does not engage in any activity other than facilitating the trading of security-based swaps on or through the security-based swap execution facility in a manner consistent with Regulation SB SEF (17 CFR 242.800 through 242.823).

(b) Except for the provisions of the Act specified in paragraph (c) of this section, a broker registered under paragraph (a) of this section that does not engage in any activity other than facilitating the trading of security-based swaps on or through the security-based swap execution facility in a manner consistent with the Regulation SB SEF (17 CFR 242.800 through 242.823) shall be exempt from the requirements of the Act and the rules and regulations thereunder that, by their terms, require, prohibit, restrict, limit, condition, or affect activities of a broker unless those requirements of the Act or any rule, regulation, or order thereunder specifies that it applies to a security-based swap execution facility.

(c) The following provisions of the Act shall apply to a broker that is a security-based swap execution facility:

(1) Section 15(b)(4) of the Act (15 U.S.C. 78o(b)(4));

(2) Section 15(b)(6) of the Act (15 U.S.C. 78o(b)(6)); and

(3) Section 17(b) of the Act (15 U.S.C. 78q(b)).

(d) A broker registered under paragraph (a) of this section that does not engage in any activity other than facilitating the trading of security-based swaps on or through the security-based swap execution facility in a manner consistent with Regulation SB SEF (17 CFR 242.800 through 242.823) shall be exempt from the Securities Investor Protection Act.

PART 242—REGULATIONS M, SHO, ATS, AC, NMS, AND SB SEF AND CUSTOMER MARGIN REQUIREMENTS FOR SECURITY FUTURES

4. The authority citation for part 242 is amended by adding the following citation to read as follows:

Authority: 15 U.S.C. 77g, 77q(a), 77s(a), 78b, 78c, 78g(c)(2), 78i(a), 78j, 78k–1(c), 78l, 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.

Sections 242.800 through 242.823 are also issued under sec. 943, Pub. L. 111–203, Section 763.

5. The heading for part 242 is revised to read as set forth above.

6. Add §§ 242.800 through 242.823 to read as follows:

* * * * *

Sec.

242.800 Definitions.
242.801 Application for registration as a security-based swap execution facility.
242.802 Amendments to application.
242.803 Supplemental material to be filed by security-based swap execution facilities.
242.804 Withdrawal from or revocation of registration for security-based swap execution facilities.
242.805 Voluntary submission of rules for Commission review and approval.
242.806 Self-certification of rules.
242.807 Trading security-based swaps pursuant to certification.
242.808 Trading security-based swaps pursuant to Commission review and approval.
242.809 Access to security-based swap execution facilities.
242.810 Compliance with core principles.
242.811 Compliance with rules.
242.812 Security-based swaps not readily susceptible to manipulation.
242.813 Monitoring of trading and trade processing.
242.814 Ability to obtain information.
242.815 Financial integrity of transactions.
242.816 Emergency authority.
242.817 Timely publication of trading information.
242.818 Recordkeeping and reporting.
242.819 Antitrust considerations.
242.820 Conflicts of interest.
242.821 Financial resources.
242.822 System safeguards.
242.823 Designation of Chief Compliance Officer of security-based swap execution facility.

* * * * *

§ 242.800 Definitions.

Terms used in this Regulation SB SEF (17 CFR 242.800 through 242.823) that appear in section 3 of the Act (15 U.S.C. 78c) have the same meaning as in section 3 of the Act (15 U.S.C. 78c) and the rules or regulations thereunder. In addition, the following definitions shall apply:

The term *affiliate* means any person that, directly or indirectly, controls, is controlled by, or is under common control with, the person.

The terms *beneficial ownership, beneficially owns,* or any derivative thereof have the same meaning, with respect to any security or other ownership interest, as set forth in § 240.13d–3 of this chapter, as if (and whether or not) such security or other ownership interest were a voting equity security registered under section 12 of the Act (15 U.S.C. 78*l*); provided that to the extent any person is a member of a group within the meaning of section 13(d)(3) under the Act (15 U.S.C. 78m(d)(3)) and § 240.13d–5(b) of this chapter, such person shall not be deemed to beneficially own such security or other ownership interest for purposes of this section, unless such person has the power to direct the vote of such security or other ownership interest.

The term *block trade* has the same meaning as § 242.900, provided however that until the Commission sets the criteria and formula for determining what constitutes a block trade under § 242.907(b), a security-based swap execution facility may set its own criteria and formula for determining what constitutes a block trade as long as such criteria and formula comply with the Core Principles relating to security-based swap execution facilities in section 3D of the Act (15 U.S.C. 78c–4) and the rules and regulations thereunder.

The term *Board* means the Board of Directors or Board of Governors of the security-based swap execution facility or any equivalent body.

The term *competent, objective personnel* means a recognized information technology firm or a qualified internal department knowledgeable of information technology systems.

The term *control, controlled by, or any derivative thereof,* for purposes of §§ 242.800 through 823, means the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise. For purposes of §§ 242.800 through 823, a person is presumed to control another person if the person:

(1) Is a director, general partner, or officer exercising executive responsibility (or having similar status or functions);

(2) Directly or indirectly has the right to vote 25 percent or more of a class of voting securities or has the power to sell or direct the sale of 25 percent or more of a class of voting securities; or

(3) In the case of a partnership, has the right to receive, upon dissolution, or has contributed, 25 percent or more of the capital.

The term *director* means any member of the Board.

The term *EDGAR Filer Manual* has the same meaning as set forth in § 232.11 of this chapter.

The term *emergency* has the same meaning as set forth in section 12(k)(7) of the Act (15 U.S.C. 78*l*(k)(7)).

The term *immediate family member* means a person's spouse, parents, children and siblings, whether by blood, marriage or adoption, or anyone residing in such person's home.

The term *independent director* means:

(1) A director who has no material relationship with:

(i) The security-based swap execution facility or any affiliate of the security-based swap execution facility; or

(ii) A participant or any affiliate of a participant.

(2) A director is not an independent director if any of the following circumstances exists:

(i) The director, or an immediate family member, is employed by or otherwise has a material relationship with the security-based swap execution facility or any affiliate thereof, or within the past three years, was employed by or otherwise had a material relationship with the security-based swap execution facility or any affiliate thereof;

(ii) (A) The director is a participant or, within the past three years, was employed by or affiliated with a participant or any affiliate thereof; or

(B) The director has an immediate family member that is, or within the past three years was, an executive officer of a participant or any affiliate thereof;

(iii) The director, or an immediate family member, has received during any twelve month period, within the past three years, payments that reasonably could affect the independent judgment or decision-making of the director from the security-based swap execution facility or any affiliate thereof or from a participant or any affiliate thereof, other than the following:

(A) Compensation for Board or Board committee services;

(B) Compensation to an immediate family member who is not an executive officer of the security-based swap execution facility or any affiliate thereof or of a participant or any affiliate thereof; or

(C) Pension and other forms of deferred compensation for prior services, not contingent on continued service;

(iv) The director, or an immediate family member, is a partner in, or controlling shareholder or executive officer of, any organization to or from which the security-based swap execution facility or any affiliate thereof made or received payments for property or services in the current or any of the past three full fiscal years that exceed two percent of the recipient's consolidated gross revenues for that year, other than the following:

(A) Payments arising solely from investments in the securities of the security-based swap execution facility or any affiliate thereof; or

(B) Payments under non-discretionary charitable contribution matching programs;

(v) The director, or an immediate family member, is, or within the past three years was, employed as an executive officer of another entity where any executive officers of the security-based swap execution facility serve on that entity's compensation committee;

(vi) The director, or an immediate family member, is a current partner of the outside auditor of the security-based swap execution facility or any affiliate thereof, or was a partner or employee of the outside auditor of the security-based swap execution facility or any affiliate thereof who worked on the audit of the security-based swap execution facility or any affiliate thereof, at any time within the past three years; or

(vii) In the case of a director that is a member of the audit committee of the security-based swap execution facility, such director (other than in his or her capacity as a member of the audit committee, the Board, or any other Board committee), accepts, directly or indirectly, any consulting, advisory, or other compensatory fee from the security-based swap execution facility or any affiliate thereof or a participant or any affiliate thereof, other than fixed amounts of pension and other forms of deferred compensation for prior service, provided such compensation is not contingent in any way on continued service.

The term *material change* means a change that a Chief Compliance Officer would reasonably need to know in order to oversee compliance of the security-based swap execution facility.

The term *material compliance matter* means any compliance matter that the Board would reasonably need to know to oversee the compliance of the security-based swap execution facility and includes, without limitation:

(1) A violation of the Federal securities laws by the security-based swap execution facility, its officers, directors, employees, or agents;

(2) A violation of the policies and procedures of the security-based swap execution facility by the security-based swap execution facility, its officers, directors, employees, or agents; or

(3) A weakness in the design or implementation of the security-based swap execution facility's policies and procedures.

The term *material systems change* means a change to automated systems that:

(1) Significantly affects existing capacity or security;

(2) In itself, raises significant capacity or security issues, even if it does not affect other existing systems;

(3) Relies upon substantially new or different technology;

(4) Is designed to provide a new service or function; or

(5) Otherwise significantly affects the operations of the security-based swap execution facility.

The term *material systems outage* means an unauthorized intrusion into any system or an event at a security-based swap execution facility that causes a problem in systems or procedures that results in:

(1) A failure to maintain accurate, time-sequenced records of all orders, quotations, and transactions that are received by, or originated on, the security-based swap execution facility;

(2) A disruption of normal operations, including switchover to back-up equipment with no possibility of near-term recovery of primary hardware;

(3) A loss of use of any system;

(4) A loss of transactions;

(5) Excessive back-ups or delays in executing trades;

(6) A loss of ability to disseminate vital information;

(7) A communication of an outage situation to other external entities;

(8) A report or referral of an event to the Board or senior management of the security-based swap execution facility;

(9) A serious threat to systems operations even though systems operations were not disrupted;

(10) A queuing of data between system components or queuing of messages to or from participants of such duration that a participant's normal activity with the security-based swap execution facility is affected; or

(11) A failure to maintain the integrity of systems that results in the entry of erroneous or inaccurate inquiries, responses, orders, quotations, other trading interest, transactions, or other information in the security-based swap execution facility or the securities markets as a whole.

The term *non-resident person* means:

(1) In the case of an individual, one who resides in or has his principal place of business in any place not in the United States;

(2) In the case of a corporation, one incorporated in or having its principal place of business in any place not in the United States; and

(3) In the case of a partnership or other unincorporated organization or association, one having its principal place of business in any place not in the United States.

The term *objective review* means an internal or external review, performed by competent, objective personnel following established audit procedures and standards, and containing a risk assessment conducted pursuant to a review schedule.

The term *participant* when used with respect to a security-based swap execution facility means a person that is permitted to directly effect transactions on the security-based swap execution facility.

The term *person associated with a participant* means any partner, officer, director, or branch manager of such participant (or any person occupying a similar status or performing similar functions), any person directly or indirectly controlling, controlled by, or under common control with such participant, or any employee of such participant.

The term *related person* when used with respect to a participant means:

(1) Any affiliate of a participant;

(2) Any person associated with a participant;

(3) Any immediate family member of a participant, or any immediate family member of the spouse of such participant, who, in each case, has the same home as the person or who is a director or officer of the security-based swap execution facility or any of its parents or subsidiaries; or

(4) Any immediate family member of a person associated with a participant, or any immediate family member of the spouse of such person, who, in each case, has the same home as the person associated with the participant or who is a director or officer of the security-based swap execution facility or any of its parents or subsidiaries.

The term *review schedule* means a schedule in which each element contained in § 242.822(a)(1) would be assessed at specific, regular intervals.

The term *tagged* means having an identifier that highlights specific information submitted to the Commission that is in the format required by the EDGAR Filer Manual, as described in Section 301 of Regulation S–T (17 CFR 232.301).

§ 242.801 Application for registration as a security-based swap execution facility.

(a) An application for registration as a security-based swap execution facility shall be filed electronically in a tagged data format with the Commission on Form SB SEF (referenced in § 249.1700 of this chapter), in accordance with the instructions contained therein. The application must include information sufficient to demonstrate compliance with the Act and rules and regulations thereunder. Form SB SEF consists of instructions, an Execution Page, and a list of Exhibits that the Commission requires in order to be able to determine whether an applicant is able to comply with the Act and rules and regulations thereunder. An application on Form SB SEF will not be considered to be complete unless the applicant has submitted, at a minimum, the Execution Page and Exhibits as required in Form SB SEF, and any other material that the Commission may require, upon request, in order to be able to determine whether an applicant is able to comply with the Act and rules and regulations thereunder. If the application is not complete, the Commission shall notify the applicant that the application will not be deemed to have been submitted for purposes of the Commission's review.

(b)(1) In connection with an application for registration furnished to the Commission under paragraph (a) of this section on or before July 31, 2014, within 360 days of the date of the filing of such application (or within such longer period as to which the applicant consents), the Commission shall:

(i) By order grant registration; or

(ii) Institute proceedings to determine whether registration should be denied. Such proceedings shall include notice of the grounds for denial under consideration and opportunity for hearing and shall be concluded within 450 days after the date on which the application for registration is furnished to the Commission under paragraph (a) of this section. At the conclusion of such proceedings, the Commission, by order, shall grant or deny such registration. The Commission may extend the time for conclusion of such proceedings for up to 90 days, if it finds good cause for such extension and publishes its reasons for so finding, or for such longer period as to which the applicant consents.

(2) In connection with an application for registration furnished to the Commission under paragraph (a) of this section after July 31, 2014, within 180 days of the date of the filing of such application (or within such longer period as to which the applicant consents), the Commission shall:

(i) By order grant registration; or

(ii) Institute proceedings to determine whether registration should be denied. Such proceedings shall include notice of the grounds for denial under consideration and opportunity for hearing and shall be concluded within 270 days after the date on which the application for registration is furnished to the Commission under paragraph (a) of this section. At the conclusion of such proceedings, the Commission, by order, shall grant or deny such registration. The Commission may extend the time for conclusion of such proceedings for up to 90 days, if it finds good cause for such extension and publishes its reasons for so finding, or for such longer period as to which the applicant consents.

(3) The Commission shall grant the registration of a security-based swap execution facility if the Commission finds that the requirements of the Act and the rules and regulations thereunder with respect to the applicant are satisfied. The Commission shall deny the registration of a security-based swap execution facility if it does not make such finding.

(c) For any application for registration as a security-based swap execution facility filed pursuant to paragraph (a) of this section on Form SB SEF (referenced in § 249.1700 of this chapter) on or before July 31, 2014, for which the applicant indicates that it would like to be considered for temporary registration pursuant to this paragraph (c), the Commission may grant temporary registration of the security-based swap execution facility that shall expire on the earlier of:

(1) The date that the Commission grants or denies registration of the security-based swap execution facility; or

(2) The date that the Commission rescinds the temporary registration of the security-based swap execution facility.

(d) A security-based swap execution facility shall designate and authorize on Form SB SEF (referenced in § 249.1700 of this chapter) an agent in the United States, other than a Commission member, official, or employee, who shall accept any notice or service of process, pleadings, or other documents in any suit, action or proceedings brought against the security-based swap execution facility to enforce the Federal securities laws or the rules or regulations thereunder.

(e) Any person applying for registration pursuant to paragraph (a) of this section that is controlled by any other person shall certify on its Form SB SEF (referenced in § 249.1700 of this chapter) and provide an opinion of counsel that any such person that controls such security-based swap execution facility will consent to and can, as a matter of law:

(1) Provide the Commission with prompt access to its books and records, to the extent such books and records are related to the activities of the security-based swap execution facility; and

(2) Submit to onsite inspection and examination by representatives of the Commission with respect to the activities of the security-based swap execution facility.

(f) Any non-resident person applying for registration pursuant to paragraph (a) of this section shall certify on its Form SB SEF (referenced in § 249.1700 of this chapter) and provide an opinion of counsel that the security-based swap execution facility can, as a matter of law:

(1) Provide the Commission with prompt access to the books and records of such security-based swap execution facility; and

(2) Submit to onsite inspection and examination by representatives of the Commission.

(g) An application for registration or any amendment thereto that is filed pursuant to Regulation SB SEF (referenced in § 249.1700 of this chapter) shall be considered a "report" filed with the Commission for purposes of sections 18(a) and 32(a) of the Act (15 U.S.C. 78r(a) and 78ff(a)) and the rules and regulations thereunder.

§ 242.802 Amendments to application.

(a) After the discovery that any information filed on Form SB SEF (referenced in § 249.1700 of this chapter), any statement therein, or any Exhibit or amendment thereto, was inaccurate when filed, the security-based swap execution facility shall file with the Commission an amendment correcting such inaccuracy promptly, but in no event later than 5 business days after such discovery.

(b)(1) The security-based swap execution facility shall file electronically with the Commission an amendment to Form SB SEF (referenced in § 249.1700 of this chapter), on Form SB SEF, within 5 business days after any action is taken that renders inaccurate, or that causes to be incomplete, any of the following:

(i) Information filed on the Execution Page of Form SB SEF (referenced in § 249.1700 of this chapter), or amendment thereto; or

(ii) Information filed as part of Exhibits C, E, G or N, or any amendments thereto.

(2) An amendment required under this paragraph (b) shall set forth the nature and effective date of the action taken and shall provide any new information and correct any information rendered inaccurate.

(c) Any security-based swap execution facility that is controlled by any other person shall file electronically with the Commission an amendment to Exhibit P to Form SB SEF (referenced in § 249.1700 of this chapter) on Form SB SEF, within 5 business days after any changes in the legal or regulatory framework of any person that controls the security-based swap execution facility that would impact the ability of or the manner in which any such person consents to or provides the Commission prompt access to its books and records, to the extent such books and records are related to the activities of the security-based swap execution facility, or impacts the Commission's ability to inspect and examine any such person with respect to the activities of the security-based swap execution facility. The amendment shall include a revised opinion of counsel pursuant to Exhibit P describing how, as a matter of law, any person that controls the security-based swap execution facility will continue to meet its obligations to consent to and provide the Commission with prompt access to its books and records, to the extent such books and records are related to the activities of the security-based swap execution facility, and to consent to and be subject to onsite inspection and examination by representatives of the Commission with respect to the activities of the security-based swap execution facility under such new legal or regulatory framework.

(d) A non-resident security-based swap execution facility shall file electronically with the Commission an amendment to Exhibit P to Form SB SEF, on Form SB SEF (referenced in § 249.1700 of this chapter), within 5 business days after any changes in legal or regulatory framework that would impact the security-based swap execution facility's ability to or the manner in which it provides the Commission prompt access to its books and records or impacts the Commission's ability to inspect and examine the security-based swap execution facility. The amendment shall include a revised opinion of counsel pursuant to Exhibit P describing how, as a matter of law, the entity will continue to meet its obligations to provide the Commission with prompt access to its books and records and to be subject to onsite inspection and examination by representatives of the Commission under such new legal or regulatory framework.

(e) Whenever the number of changes to be reported in an amendment, or the number of amendments filed, are so great that the purpose of clarity will be promoted by the filing of a complete new statement and exhibits, a security-based swap execution facility may, at its election, or shall, upon request of any representative of the Commission, file as an amendment a complete new statement together with all exhibits which are prescribed to be filed in connection with Form SB SEF (referenced in § 249.1700 of this chapter).

(f) Within 60 days of the end of its fiscal year, a security-based swap execution facility shall file an amendment to its Form SB SEF (referenced in § 249.1700 of this chapter), which shall update the Form SB SEF in its entirety. Each exhibit to the amended Form SB SEF shall be up to date as of the end of the latest fiscal year of the security-based swap execution facility.

§ 242.803 Supplemental material to be filed by security-based swap execution facilities.

(a) A registered security-based swap execution facility, or a security-based swap execution facility exempted from such registration pursuant to section 3D(e) of the Act (15 U.S.C. 78c–4(e)), shall file electronically with the Commission any material relating to the trading of security-based swaps (including notices, circulars, bulletins, lists, and periodicals) issued or made generally available to participants. Such material shall be filed with the Commission upon issuing or making such material available to the participants.

(b) If the information required to be filed under paragraph (a) of this section is available continuously on an Internet Web site controlled by a security-based swap execution facility, in lieu of filing such information with the Commission, such security-based swap execution facility may:

(1) Indicate the location of the Internet Web site where such information may be found; and

(2) Certify that the information available at such location is accurate as of its date.

§ 242.804 Withdrawal from or revocation of registration for security-based swap execution facilities.

(a) A registered security-based swap execution facility may withdraw from registration by filing a written notice of withdrawal with the Commission. The security-based swap execution facility shall designate on its notice of withdrawal a person associated with the security-based swap execution facility to serve as the custodian of the security-based swap execution facility's books and records. Prior to filing a notice of withdrawal, a security-based swap execution facility shall file an amended Form SB SEF (referenced in § 249.1700 of this chapter) to update any inaccurate information.

(b) A notice of withdrawal from registration filed by a security-based

swap execution facility shall become effective for all matters (except as provided in this paragraph (b)) on the 60th day after the filing thereof with the Commission, within such longer period of time as to which such security-based swap execution facility consents or the Commission, by order, may determine as necessary or appropriate in the public interest or for the protection of investors, or within such shorter period of time as the Commission may determine.

(c) A notice of withdrawal that is filed pursuant to this rule shall be considered a "report" filed with the Commission for purposes of sections 18(a) and 32(a) of the Act (15 U.S.C. 78r(a) and 78ff(a)), and the rules and regulations thereunder.

(d) If the Commission finds, on the record after notice and opportunity for hearing, that any registered security-based swap execution facility has obtained its registration by making any false or misleading statements with respect to any material fact or has violated or failed to comply with any provision of the Federal securities laws and the rules and regulations thereunder, the Commission, by order, may revoke the registration. Pending final determination of whether any registration shall be revoked, the Commission, by order, may suspend such registration, if such suspension appears to the Commission, after notice and opportunity for hearing, to be necessary or appropriate in the public interest or for the protection of investors.

(e) If the Commission finds that a registered security-based swap execution facility is no longer in existence or has ceased to do business in the capacity specified in its application for registration, the Commission, by order, may cancel the registration.

§ 242.805 Voluntary submission of rules for Commission review and approval.

(a) *Request for approval of rules.* A registered security-based swap execution facility may request that the Commission approve a new rule or rule amendment prior to implementation of the new rule or rule amendment or, if the request was initially submitted under § 242.806 or 242.807, subsequent to implementation of the new rule or rule amendment. A request for approval shall:

(1) Be filed electronically with the Commission in a format specified by the Commission;

(2) Set forth the text of the new rule or rule amendment (in the case of a rule amendment, deletions and additions must be indicated);

(3) Describe the proposed effective date of the new rule or rule amendment and any action taken or anticipated to be taken to adopt the proposed rule by the registered security-based swap execution facility or by its Board, or by any committee thereof, and cite the rules of the registered security-based swap execution facility that authorize the adoption of the proposed rule change;

(4) Explain the operation, purpose, and effect of the new rule or rule amendment, including, as applicable, a description of the anticipated benefits to market participants or others, any potential anticompetitive effects on market participants or others, and how the rule fits into the registered security-based swap execution facility's framework of regulation;

(5) Certify that the registered security-based swap execution facility has published on its Web site a notice of pending new rule or rule amendment with the Commission and a copy of the submission, concurrent with the filing of the submission with the Commission;

(6) Include the documentation relied on to establish the basis for compliance with the applicable provisions of the Act and Commission rules and regulations thereunder, including section 3D(d) of the Act (15 U.S.C. 78c–4(d)) and the rules and regulations thereunder;

(7) Provide additional information that may be beneficial to the Commission in analyzing the new rule or rule amendment. If a proposed rule affects, directly or indirectly, the application of any other rule of the registered security-based swap execution facility, the pertinent text of any such rule must be set forth and the anticipated effect described;

(8) Describe briefly any substantive opposing views expressed to the registered security-based swap execution facility by the Board or committee members, participants, or market participants with respect to the new rule or rule amendment that were not incorporated into the new rule or rule amendment;

(9) Identify any Commission rule or regulation that the Commission may need to amend, or sections of the Act or the rules or regulations thereunder that the Commission may need to interpret, in order to approve the new rule or rule amendment. To the extent that such an amendment or interpretation is necessary to accommodate a new rule or rule amendment, the submission should include a reasoned analysis supporting the proposed amendment or interpretation;

(10) In the case of proposed amendments to the terms and conditions of a security-based swap, include a written statement verifying that the registered security-based swap execution facility has undertaken a due diligence review of the legal conditions, including conditions relating to contractual and intellectual property rights, that may materially affect the trading of the security-based swap; and

(11) A request for confidential treatment, if appropriate, as permitted pursuant to the applicable provisions of the Freedom of Information Act, 5 U.S.C. 552, and Commission rules and regulations thereunder, 17 CFR 200.83.

(b) *Standard for review and approval.* The Commission shall approve a new rule or rule amendment unless the new rule or rule amendment is inconsistent with the Act or Commission rules or regulations.

(c) *Forty-five day review.* (1) All rules submitted for Commission approval under paragraph (a) of this section shall be deemed approved by the Commission 45 days after receipt by the Commission, or at the conclusion of such extended period as provided under paragraph (d) of this section, unless the registered security-based swap execution facility is notified otherwise within the applicable period, if:

(i) The submission complies with the requirements of paragraph (a) of this section; and

(ii) The registered security-based swap execution facility does not amend the new rule or rule amendment or supplement the submission, except as requested by the Commission, during the pendency of the review period. Any amendment or supplementation not requested by the Commission will be treated as the submission of a new filing under this section.

(d) *Extension of time for review.* The Commission may further extend the review period in paragraph (c) of this section for any approval request for:

(1) An additional 45 days, if the new rule or rule amendment raises novel or complex issues that require additional time for review, is of major economic significance, the submission is incomplete, or the requestor does not respond completely to the Commission's questions in a timely manner, in which case, the Commission shall notify the submitting registered security-based swap execution facility within the initial 45-day review period and shall briefly describe the nature of the specific issues for which additional time for review shall be required; or

(2) Any period, beyond the additional 45 days provided in paragraph (d)(1) of this section, to which the registered security-based swap execution facility agrees in writing.

(e) *Notice of non-approval.* Any time during its review under this section, the Commission may notify the registered security-based swap execution facility that it will not, or is unable to, approve the new rule or rule amendment. This notification will briefly specify the nature of the issues raised and the specific provision of the Act or Commission rules or regulations, including the form or content requirements of this section, with which the new rule or rule amendment is inconsistent or appears to be inconsistent with the Commission rules or regulations.

(f) *Effect of non-approval.* (1) Notification to a registered security-based swap execution facility under paragraph (e) of this section shall not prevent the registered security-based swap execution facility from subsequently submitting a revised version of the new rule or rule amendment for the Commission's review and approval or from submitting the new rule or rule amendment as initially proposed in a supplemented submission. The revised submission will be reviewed without prejudice.

(2) Notification to a registered security-based swap execution facility under paragraph (e) of this section of the Commission's determination not to approve the new rule or rule amendment of the registered security-based swap execution facility shall be presumptive evidence that the registered security-based swap execution facility may not truthfully certify the same, or substantially the same, proposed rule or rule amendment under § 242.806.

(g) *Expedited approval.* Notwithstanding the provisions of paragraph (c) of this section, a new rule or rule amendment, including proposed changes to the terms and conditions of a security-based swap, that is consistent with the Act and Commission rules and regulations and with standards approved or established by the Commission may be approved by the Commission at such time and under such conditions as the Commission shall specify in the written notification; provided, however, that the Commission may, at any time, alter or revoke the applicability of such a notice to any particular product or rule amendment.

§ 242.806 Self-certification of rules.

(a) *Required certification.* A registered security-based swap execution facility shall comply with the following conditions prior to implementing any rule that has not obtained Commission approval under § 242.805:

(1) The registered security-based swap execution facility has filed its submission electronically in a format specified by the Commission.

(2) The registered security-based swap execution facility has provided to the Commission a certification that it published on its Web site a notice of pending certification with the Commission and a copy of the submission, concurrent with the filing of a submission with the Commission. Information that the registered security-based swap execution facility seeks to keep confidential may be redacted from the documents published on its Web site but must be republished consistent with any determination made pursuant to the applicable provisions of the Freedom of Information Act, 5 U.S.C. 552, and Commission rules and regulations thereunder, 17 CFR 200.83.

(3) The Commission has received the submission not later than the opening of business on the business day that is 10 business days prior to the registered security-based swap execution facility's proposed implementation of the rule or rule amendment; provided, however, that if a security-based swap execution facility implements any rule or rule amendment in the exercise of its emergency authority pursuant to § 242.816, it shall file such rule or rule amendment with the Commission pursuant to this paragraph (a) prior to the implementation of such rule or rule amendment, or, if not practicable, within 24 hours after implementation of such emergency rule or rule amendment.

(4) The Commission has not stayed the submission pursuant to paragraph (c) of this section.

(5) The rule submission includes:

(i) The text of the rule (in the case of a rule amendment, deletions, and additions must be indicated);

(ii) The date of intended implementation;

(iii) A certification by the registered security-based swap execution facility that the rule complies with the Act and Commission rules and regulations thereunder;

(iv) The documentation relied on to establish the basis for compliance with the applicable provisions of the Act and Commission rules and regulations thereunder, including section 3D(d) of the Act (15 U.S.C. 78c–4(d)) and the rules and regulations thereunder;

(v) A brief explanation of any substantive opposing views expressed to the registered security-based swap execution facility by the Board or committee members, participants, or market participants that were not incorporated into the rule, or a statement that no such opposing views were expressed;

(vi) A request for confidential treatment, if appropriate, as permitted pursuant to the applicable provisions of the Freedom of Information Act, 5 U.S.C. 552, and Commission rules and regulations thereunder, 17 CFR 200.83; and

(vii) For amendments to the terms and conditions of a security-based swap, a written statement verifying that the registered security-based swap execution facility has undertaken a due diligence review of the legal conditions, including conditions relating to contractual and intellectual property rights, that may materially affect the trading of the product.

(6) The registered security-based swap execution facility has provided, upon request of any representative of the Commission, additional evidence, information, or data that may be beneficial to the Commission in conducting a due diligence assessment of the filing and the registered security-based swap execution facility's compliance with any of the requirements of the Act or Commission rules or regulations thereunder.

(b) *Review by the Commission.* The Commission shall have 10 business days to review the new rule or rule amendment before the new rule or rule amendment is deemed certified and can be made effective, unless the Commission notifies the registered security-based swap execution facility during the 10-business day review period that it intends to issue a stay of the certification under paragraph (c) of this section.

(c) *Stay.* (1) *Stay of certification of new rule or rule amendment.* The Commission may stay the certification of a new rule or rule amendment submitted pursuant to paragraph (a) of this section by issuing a notification informing the registered security-based swap execution facility that the Commission is staying the certification of the new rule or rule amendment on the grounds that the new rule or rule amendment presents novel or complex issues that require additional time to analyze, the new rule or rule amendment is accompanied by an inadequate explanation, or the new rule or rule amendment is potentially inconsistent with the Act or Commission rules or regulations

thereunder. The Commission will have 90 days from the date of the notification to conduct a review.

(2) *Public comment.* The Commission shall provide a 30-day comment period within the 90-day review period while the stay is in effect as described in paragraph (c)(1) of this section. The Commission shall publish a notice of the 30-day comment period on the Commission's Web site. Comments from the public shall be submitted as specified in that notice.

(3) *Expiration of a stay of certification of new rule or rule amendment.* A new rule or rule amendment subject to a stay pursuant to paragraph (c) of this section shall become effective, pursuant to the certification, at the expiration of the 90-day review period described in paragraph (c)(1) of this section unless the Commission withdraws the stay prior to that time or the Commission notifies the registered security-based swap execution facility during the 90-day review period that it objects to the certification on the grounds that the new rule or rule amendment is inconsistent with the Act or Commission rules or regulations thereunder.

(d) Notwithstanding paragraph (a) of this section, a registered security-based swap execution facility may place the following new rules or rule amendments into effect on the following business day without certification to the Commission if the following conditions are met:

(1) The rule is limited to corrections of typographical errors, renumbering, periodic routine updates to identifying information about approved entities, and other such non-substantive revisions of the terms and conditions of a security-based swap that have no effect on the economic characteristics of the security-based swap; and

(2) The registered security-based swap execution facility provides to the Commission at least weekly a summary notice of all rule amendments made effective pursuant to this paragraph during the preceding week. Such notice must be labeled "Weekly Notification of Rule Amendments" and need not be filed for weeks during which no such actions have been taken. One copy of each such submission shall be furnished electronically in a format specified by the Commission.

(e) Notwithstanding paragraph (a) of this section, a registered security-based swap execution facility may place the following new rules or rule amendments into effect without certification or notice to the Commission if the following conditions are met:

(1) The rule governs:

(i) *Administrative procedures.* The organization and administrative procedures of a security-based swap execution facility's governing bodies, such as the Board, officers, and committees, but not any of the following: Voting requirements, Board or committee composition requirements or procedures, decision making procedures, use or disclosure of material non-public information gained through the performance of official duties, or requirements relating to conflicts of interest; or

(ii) *Administration.* The routine, daily administration, direction and control of employees, requirements relating to gratuity and similar funds, but not any of the following: Guaranty, reserves, or similar funds; declaration of holidays; and changes to facilities housing the market; and

(2) The registered security-based swap execution facility maintains documentation regarding all changes to rules and posts all such rule changes on its Web site.

§ 242.807 Trading security-based swaps pursuant to certification.

(a) A registered security-based swap execution facility shall comply with the submission requirements of this section prior to trading a security-based swap that has not been approved under § 242.808. A submission shall comply with the following conditions:

(1) The registered security-based swap execution facility has filed its submission electronically in a format specified by the Commission;

(2) The Commission has received the submission by the opening of business on the business day preceding the day on which the security-based swap would begin trading;

(3) The Commission has not stayed the submission pursuant to paragraph (c) of this section; and

(4) The submission includes:

(i) A copy of the terms and conditions of the security-based swap;

(ii) The intended date on which the security-based swap may begin trading;

(iii) A certification by the registered security-based swap execution facility that the security-based swap to be traded complies with the Act and Commission rules and regulations thereunder;

(iv) The documentation relied on to establish the basis for compliance with the Act and the rules and regulations thereunder, including section 3D(d) of the Act (15 U.S.C. 78c–4(d)) and the rules and regulations thereunder;

(v) A written statement verifying that the registered security-based swap execution facility has undertaken a due diligence review of the legal conditions, including legal conditions that relate to contractual and intellectual property rights, that may materially affect the trading of the security-based swap;

(vi) A certification that the registered security-based swap execution facility published on its Web site a notice of pending certification with the Commission and a copy of the submission, concurrent with the filing of the submission with the Commission. Information that the registered security-based swap execution facility seeks to keep confidential may be redacted from the documents published on its Web site, but must be republished consistent with any determination made pursuant to the applicable provisions of the Freedom of Information Act, 5 U.S.C. 552, and Commission rules and regulations thereunder, 17 CFR 200.83; and

(vii) A request for confidential treatment, if appropriate, as permitted pursuant to the applicable provisions of the Freedom of Information Act, 5 U.S.C. 552, and Commission rules and regulations thereunder, 17 CFR 200.83.

(b) A registered security-based swap execution facility, upon request of any representative of the Commission, shall provide any additional evidence, information, or data that demonstrates that the security-based swap meets, initially or on a continuing basis, all of the requirements of the Act and Commission rules and regulations thereunder.

(c) *Stay.* (1) The Commission may stay the certification of a security-based swap pursuant to paragraph (a) of this section by issuing a notification informing the registered security-based swap execution facility that the Commission is staying the certification on the grounds that the security-based swap proposed to begin trading presents novel or complex issues that require additional time to analyze, the certification is accompanied by an inadequate explanation or the proposed security-based swap is potentially inconsistent with the Act or Commission rules or regulations thereunder. The Commission will have 90 days from the date of the notification to conduct the review.

(2) *Public comment.* The Commission shall provide a 30-day comment period, within the 90-day review period while the stay is in effect as described in paragraph (c)(1) of this section. The Commission shall publish a notice of the 30-day comment period on the Commission's Web site. Comments from the public shall be submitted as specified in that notice.

(3) *Expiration of a stay.* A proposed security-based swap subject to a stay pursuant to paragraph (c) of this section shall become effective, pursuant to the certification, at the expiration of the 90-day review period described in paragraph (c)(1) of this section unless the Commission withdraws the stay prior to that time or the Commission notifies the registered security-based swap execution facility during the 90-day review period that it objects to the proposed certification on the grounds that it is inconsistent with the Act or Commission rules or regulations thereunder.

§ 242.808 Trading security-based swaps pursuant to Commission review and approval.

(a) A registered security-based swap execution facility may request that the Commission approve a security-based swap prior to trading such security-based swap or, if a security-based swap was initially submitted under § 242.807, subsequent to the commencement of trading such security-based swap. A submission requesting approval shall be filed electronically with the Commission in a format specified by the Commission and include:

(1) A copy of the terms and conditions of the security-based swap;

(2) The documentation relied on to establish the basis for compliance with the Act and rules and regulations thereunder, including section 3D(d) of the Act (15 U.S.C. 78c–4(d)) and the rules and regulations thereunder;

(3) A written statement verifying that the registered security-based swap execution facility has undertaken a due diligence review of the legal conditions, including legal conditions that relate to contractual and intellectual property rights, that may materially affect the trading of the security-based swap;

(4) A request for confidential treatment, if appropriate, as permitted pursuant to the applicable provisions of the Freedom of Information Act, 5 U.S.C. 552, and Commission rules and regulations thereunder, 17 CFR 200.83;

(5) A certification that the registered security-based swap execution facility has published on its Web site a notice of pending request for approval with the Commission and a copy of the submission, concurrent with the filing of a submission with the Commission. Information that the registered security-based swap execution facility seeks to keep confidential may be redacted from the documents published on its Web site, but must be republished consistent with any determination made pursuant to the applicable provisions of the Freedom of Information Act, 5 U.S.C. 552, and Commission rules or regulations thereunder, 17 CFR 200.83; and

(b) A registered security-based swap execution facility, upon request of any representative of the Commission, shall provide additional evidence, information, or data that demonstrates that the security-based swap meets, initially or on a continuing basis, all of the requirements of the Act and Commission rules or regulations thereunder.

(c) *Standard for review and approval.* The Commission shall approve a security-based swap unless the terms and conditions of such security-based swap are inconsistent with the Act or Commission rules or regulations thereunder.

(d) *Forty-five day review.* All security-based swaps submitted for Commission approval under this section shall be deemed approved by the Commission 45 days after receipt by the Commission or at the conclusion of an extended period as provided under paragraph (e) of this section, unless the registered security-based swap execution facility is notified otherwise within the applicable period, if:

(1) The submission complies with the requirements of paragraph (a) of this section; and

(2) The registered security-based swap execution facility making the submission does not amend the terms and conditions of the security-based swap or supplement its request for approval during that period, except as requested by the Commission to correct typographical errors, renumber, or make other non-substantive revisions, during that period. Any voluntary, substantive amendment by the registered security-based swap execution facility shall be treated as a new submission under this section.

(e) *Extension of time.* The Commission may extend the 45-day review period in paragraph (d) of this section for:

(1) An additional 45 days, if the proposed security-based swap raises novel or complex issues that require additional time for review, in which case the Commission shall notify the registered security-based swap execution facility within the initial 45-day review period and shall briefly describe the nature of the specific issues for which additional time for review is required; or

(2) Any extended review period to which the registered security-based swap execution facility agrees in writing.

(f) *Notice of non-approval.* The Commission at any time during its review under this section may notify the registered security-based swap execution facility that it will not, or is unable to, approve the security-based swap. This notification will briefly specify the nature of the issues raised and the specific provision of the Act or Commission rules or regulations thereunder, including the form or content requirements of paragraph (a) of this section, with which the security-based swap is inconsistent, appears to be inconsistent, or is potentially inconsistent.

(g) *Effect of non-approval.* (1) Notification to a registered security-based swap execution facility under paragraph (f) of this section of the Commission's determination not to approve a security-based swap shall not prejudice the registered security-based swap execution facility from subsequently submitting a revised version of the security-based swap for Commission approval or from submitting the security-based swap as initially proposed pursuant to a supplemented submission.

(2) Notification to a registered security-based swap execution facility under paragraph (f) of this section of the Commission's inability to approve the security-based swap shall be presumptive evidence that the registered security-based swap execution facility may not truthfully certify under § 242.807 that the same, or substantially the same, security-based swap complies with the Act or Commission rules and regulations thereunder.

§ 242.809 Access to security-based swap execution facilities.

(a) A security-based swap execution facility shall permit a person to become a participant in the security-based swap execution facility only if such person is registered with the Commission as a security-based swap dealer, major security-based swap participant, or broker (as defined in section 3(a)(4) of the Act, 15 U.S.C. 78c(a)(4)), or if such person is an eligible contract participant (as defined in section 3(a)(65) of the Act, 15 U.S.C. 78c(a)(65)).

(b) A security-based swap execution facility shall permit all eligible persons that meet the requirements for becoming a participant in the security-based swap execution facility under paragraph (a) of this section and the security-based swap execution facility's rules to become participants of the security-based swap execution facility, consistent with the requirements for providing impartial access in section 3D(d)(6) of the Act (15 U.S.C. 78c–4(d)(6)) and § 242.811(b); provided, however, that a security-based

swap execution facility may choose to not permit any eligible contract participants that are not registered with the Commission as a security-based swap dealer, major security-based swap participant, or broker (as defined in section 3(a)(4) of the Act, 15 U.S.C. 78c(a)(4)) to become participants in the security-based swap execution facility.

(c) A security-based swap execution facility shall establish rules setting forth requirements for an eligible person to become a participant in the security-based swap execution facility consistent with the security-based swap execution facility's obligations under the Act and the rules and regulations thereunder. Such rules must require a participant, at a minimum, to:

(1) Be a member of, or have an arrangement with a member of, a registered clearing agency to clear trades in the security-based swaps that are subject to mandatory clearing pursuant to section 3C(a)(1) of the Act (15 U.S.C. 78c–3(a)(1)) and entered into by the participant on the security-based swap execution facility;

(2)(i) Meet the minimum financial responsibility and recordkeeping and reporting requirements imposed by the Commission by virtue of its registration as a security-based swap dealer, major security-based swap participant, or broker; or

(ii) In the case of an eligible contract participant that is not registered with the Commission as a security-based swap dealer, major security-based swap participant, or broker, meet the recordkeeping and reporting requirements that the security-based swap execution facility shall establish pursuant to § 242.813;

(3) Agree to comply with the rules, policies, and procedures of the security-based swap execution facility; and

(4) Consent to the disciplinary procedures of the security-based execution facility for violations of the security-based swap execution facility's rules.

(d)(1) A security-based swap execution facility that permits an eligible contract participant that is not registered as a security-based swap dealer, major security-based swap participant or broker to become a participant in the security-based swap execution facility pursuant to this section shall establish, document, and maintain a system of risk management controls and supervisory procedures reasonably designed to manage the financial, regulatory, and other risks of this business activity.

(2) The risk management controls and supervisory procedures for granting access to eligible contract participants that are not registered as a security-based swap dealer, major security-based swap participant, or broker as participants of the security-based swap execution facility shall be reasonably designed to ensure compliance with all regulatory requirements.

§ 242.810 Compliance with core principles.

(a) To be registered, and maintain registration, as a security-based swap execution facility, a security-based swap execution facility shall comply with:

(1) The Core Principles described in section 3D of the Act (15 U.S.C. 78c–4) and the rules and regulations thereunder; and

(2) The requirements of this rule and any other requirement that the Commission may impose by rule or regulation.

(b) A security-based swap execution facility shall establish:

(1) Rules that provide for the equitable allocation of reasonable dues, fees, and other charges among its participants and any other users of its system;

(2) Rules and systems that are not designed to permit unfair discrimination among its participants and any other persons using its system;

(3) Rules that promote just and equitable principles of trade; and

(4) Rules to provide, in general, a fair procedure for disciplining participants for violations of the rules of the security-based swap execution facility.

(c) A security-based swap execution facility shall not use for non-regulatory purposes any confidential information it collects or receives, from or on behalf of any person, in connection with the security-based swap execution facility's regulatory obligations.

§ 242.811 Compliance with rules.

(a) A security-based swap execution facility shall:

(1) Establish and enforce compliance with any rule established by such security-based swap execution facility, including:

(i) The terms and conditions of the security-based swaps traded or processed on or through the security-based swap execution facility; and

(ii) Any limitation on access to the security-based swap execution facility;

(2) Establish and enforce trading, trade processing, and participation rules that will deter abuses and have the capacity to detect, investigate, and enforce those rules, including means:

(i) To provide market participants with impartial access to the market; and

(ii) To capture information that may be used in establishing whether rule violations have occurred; and

(3) Establish rules governing the operation of the security-based swap execution facility, including rules specifying trading procedures to be used in entering and executing orders traded or posted on the security-based swap execution facility, including block trades.

(b) A security-based swap execution facility shall:

(1) Establish fair, objective, and not unreasonably discriminatory standards for granting impartial access to trading on the security-based swap execution facility, which standards shall include a requirement that each participant of the security-based swap execution facility submit to the oversight (including the disciplinary procedures of paragraph (g) of this section) of the security-based swap execution facility, with respect to the participant's trading on the facility, as a condition of becoming a participant in such security-based swap execution facility;

(2) Not unreasonably prohibit or limit any person in respect to access to the services offered by such security-based swap execution facility by applying the standards established under paragraph (b)(1) of this section in an unfair or unreasonably discriminatory manner;

(3) Make and keep records of:

(i) All grants of access, including, for all participants, the basis for granting such access; and

(ii) All denials or limitations of access for each applicant or participant (as applicable), and the reasons for denying or limiting access;

(4) Report the information required regarding grants, denials, and limitations of access on Form SB SEF (referenced in § 249.1700 of this chapter) and in the annual compliance report of the Chief Compliance Officer pursuant to § 242.823(c); and

(5) Establish a fair process for the review of any prohibition or limitation on access with respect to a participant or any refusal to grant access with respect to an applicant.

(c) A security-based swap execution facility shall establish and enforce compliance with rules concerning the terms and conditions of the security-based swaps traded on the security-based swap execution facility.

(1) A security-based swap execution facility shall establish a swap review committee to determine:

(i) The security-based swaps that shall trade on the security-based swap execution facility; and

(ii) The security-based swaps that shall no longer trade on the security-based swap execution facility.

(2) The composition of the swap review committee shall provide for the

fair representation of participants of the security-based swap execution facility and other market participants, such that each class of participant and other market participants shall be given the right to participate in such swap review committee and that no single class of participant or category of market participant shall predominate. The rules of the security-based swap execution facility shall stipulate the method by which such representation shall be chosen by the Board.

(3) The security-based swap execution facility shall establish criteria that the swap review committee shall consider in determining which security-based swaps shall trade on the security-based swap execution facility.

(4) The swap review committee shall periodically review, on at least a quarterly basis, each security-based swap trading on the security-based swap execution facility to determine whether the trading characteristics of each security-based swap justify a change to the trading platform for each such security-based swap. In addition to the factors set forth in paragraph (c)(3) of this section in making such a determination, the swap review committee shall consider whether:

(i) The liquidity in each security-based swap is at an appropriate level for the security-based swap's trading platform on which it trades; and

(ii) Such security-based swap would be more suited for trading on a different type of platform, including a platform that provides for increased price transparency for participants entering orders, requests for quotations, responses, quotations, or other trading interest. The first review shall not be earlier than 120 days after the initiation of trading for a given security-based swap.

(5) The swap review committee shall report decisions on each security-based swap promptly to the Chief Compliance Officer and annually to the regulatory oversight committee.

(d) A security-based swap execution facility shall establish and enforce rules governing the procedures for trading on the security-based swap execution facility, including, but not limited to, rules concerning:

(1) Doing business on the security-based swap execution facility;

(2) The types of orders, requests for quotations, responses, quotations, or other trading interest that will be available on the security-based swap execution facility;

(3) The manner in which trading interest, including orders, requests for quotations, responses, or quotations will be handled on the security-based swap execution facility. The rules of a security-based swap execution facility shall provide for fair treatment of all trading interest;

(4) The manner in which price transparency for participants entering orders, requests for quotations, responses, quotations, or other trading interest into the system will be promoted;

(5) The manner in which trading interest, including orders, requests for quotations, responses, quotations, and transaction data will be disseminated, whether to participants of the security-based swap execution facility or otherwise, and whether for a fee or otherwise;

(6) Prohibited trading practices;

(7) The prevention of the entry of orders, requests for quotations, responses, quotations, or other trading interest that may result in a trade that is clearly erroneous with respect to the terms of the trade; the fair and non-discriminatory manner of handling any trade that is clearly erroneous; and the resolution of any disputes concerning a clearly erroneous trade;

(8) Trading halts in any security-based swap, which rules shall include procedures for halting trading in a security-based swap when trading has been halted or suspended in the underlying security or securities pursuant to the rules or an order of a regulatory authority with authority over the underlying security or securities;

(9) The manner in which block trades will be handled, if different from the handling of non-block trades; and

(10) Any other rules concerning trading on the security-based swap execution facility.

(e) A security-based swap execution facility that operates a request-for-quote platform shall create and disseminate through the security-based swap execution facility a composite indicative quote for security-based swaps traded on or through such system, which shall be made available to all participants. The composite indicative quote shall include both composite indicative bids and composite indicative offers.

(f) A security-based swap execution facility shall establish and enforce rules concerning:

(1) The reporting of trades executed on the security-based swap execution facility to a clearing agency, if the transaction is subject to clearing; and

(2) The procedures for the processing of transactions in security-based swaps that occur on or though the security-based swap execution facility, including, but not limited to, procedures to resolve any disputes concerning the execution of a trade.

(g) A security-based swap execution facility shall establish rules and procedures concerning the disciplining of participants, including, but not limited to, rules:

(1) Authorizing its staff to recommend and take disciplinary action for violations of the rules of the security-based swap execution facility;

(2) Specifying the sanctions that may be imposed upon participants for violations of the rules of the security-based swap execution facility such that each sanction is commensurate with the corresponding violation; and

(3) Establishing fair and non-arbitrary procedures for any disciplinary process and appeal thereof.

(h) A security-based swap execution facility shall:

(1) Make and keep records of all disciplinary proceedings, sanctions imposed, and appeals thereof; and

(2) Disclose all disciplinary actions taken annually on an amendment to Form SB SEF and in the security-based swap execution facility's annual compliance report of the Chief Compliance Officer required pursuant to § 242.823(c). Such report shall include information summarizing any disciplinary action taken and the reasons for such action.

(i) A security-based swap execution facility shall establish rules and procedures to assure that information to be used to determine whether rule violations have occurred is captured and retained in a timely manner.

(j) A security-based swap execution facility shall:

(1) Have the capacity to capture information that may be used in establishing whether rule violations have occurred, including through the use of automated surveillance systems as set forth in § 242.813(b);

(2) Maintain appropriate resources to fulfill its obligations under this section; and

(3) Investigate possible rule violations.

§ 242.812 Security-based swaps not readily susceptible to manipulation.

(a) A security-based swap execution facility shall permit trading only in security-based swaps that are not readily susceptible to manipulation.

(b) Prior to permitting the trading of any security-based swap, a security-based swap execution facility's swap review committee shall have determined, after taking into account all of the terms and conditions of the security-based swap and the markets for the security-based swap and any underlying security or securities, that such security-based swap is not readily susceptible to manipulation.

(c) *Periodic Review.* The rules of a security-based swap execution facility shall require that, after commencement of trading of a security-based swap, the swap review committee shall periodically review the trading in the security-based swap. If the swap review committee cannot determine, after taking into account all of the terms and conditions of the security-based swap, the markets for the security-based swap and any underlying security or securities, and the trading in the security-based swap, that such security-based swap is not readily susceptible to manipulation, the security-based swap execution facility shall no longer permit the trading of such security-based swap.

§ 242.813 Monitoring of trading and trade processing.

(a) A security-based swap execution facility shall:

(1) Establish and enforce rules, terms and conditions defining, or specifications detailing:

(i) Trading procedures to be used in entering and executing orders traded on or through the facilities of the security-based swap execution facility; and

(ii) Procedures for trade processing of security-based swaps on or through the facilities of the security-based swap execution facility; and

(2) Monitor trading in security-based swaps to prevent manipulation, price distortion, and disruptions of the delivery or cash settlement practices and procedures, including methods for conducting real-time monitoring of trading and comprehensive and accurate trade reconstructions.

(b) A security-based swap execution facility shall have the capacity and appropriate resources to electronically monitor trading in security-based swaps on its market by establishing an automated surveillance system, including through real-time monitoring of trading and use of automated alerts, that is designed to:

(1) Detect and deter any fraudulent or manipulative acts or practices, including insider trading or other unlawful conduct or any violation of the rules of the security-based swap execution facility that has occurred or is occurring;

(2) Detect and deter market distortions or disruptions of trading that may impact the entry and execution of trading interests or the processing of trading interests on or through the security-based swap execution facility;

(3) Conduct real-time monitoring of trading to provide for comprehensive and accurate trade reconstruction; and

(4) Collect and assess data to allow the security-based swap execution facility to respond promptly to market abuses or disruptions.

(c) A security-based swap execution facility shall establish and enforce rules that require any participant that enters any order, request for quotation, response, quotation, or other trading interest, or executes any transaction on the security-based swap execution facility, to:

(1) Maintain books and records of any such order, request for quotation, response, quotation or other trading interest, or transaction, and of any position in any security-based swap that is the result of any such order, request for quotation, response, quotation, other trading interest, or transaction; and

(2) Provide prompt access to such books and records to the security-based swap execution facility and to the Commission.

(d) A security-based swap execution facility shall establish and maintain procedures to investigate possible rule violations, to prepare reports concerning the findings and recommendations of any such investigations, and to take corrective action, as necessary.

§ 242.814 Ability to obtain information.

(a) A security-based swap execution facility shall establish and enforce rules requiring its participants to:

(1) Furnish to the security-based swap execution facility, upon request, and in the form and manner prescribed by the security-based swap execution facility, any information necessary to permit the security-based swap execution facility to perform its responsibilities under this section, including, without limitation, surveillance, investigations, examinations and discipline of participants; such information may include, without limitation, financial information, books, accounts, records, files, memoranda, correspondence, and any other information pertaining to orders, requests for quotations, responses, quotations, or other trading interest entered and transactions executed on or through the security-based swap execution facility;

(2) Cooperate with the security-based swap execution facility and allow access by the security-based swap execution facility, at such reasonable times as the security-based swap execution facility may request, to examine the books and records of the participant or to obtain or verify information related to orders, requests for quotation, responses, quotations, or other trading interest entered and transactions executed on or through its facilities; and

(3) Cooperate with any representative of the Commission and allow access by any representative of the Commission, at such reasonable times as any representative of the Commission may request, to examine the books and records of the participant or to obtain or verify other information related to orders, requests for quotation, responses, quotations, or other trading interest entered and transactions executed on or through its facilities.

(b) A security-based swap execution facility shall:

(1) Cooperate with any representative of the Commission and allow access by any representative of the Commission, at such reasonable times as any representative of the Commission may request, to:

(i) Examine the books and records required to be kept by the security-based swap execution facility pursuant to § 242.818; and

(ii) Obtain or verify other information related to orders, requests for quotations, responses, quotations, or other trading interest entered and transactions executed on or through its facilities;

(2) Upon request of any representative of the Commission, promptly furnish to the possession of such representative copies of any documents, in such form and manner acceptable to such representative, that the security-based swap execution facility possesses or has access to pursuant to paragraph (a) of this section;

(3) Have the capacity to carry out such international information-sharing agreements as the Commission may require; and

(4) Certify at the time of registration on Form SB SEF, and annually thereafter as part of the annual compliance report described in § 242.823, that the security-based swap execution facility has the capacity to fulfill its obligations under any international information-sharing agreements to which it is a party as of the date of such certification.

§ 242.815 Financial integrity of transactions.

(a) A security-based swap execution facility shall establish and enforce rules and procedures for ensuring the financial integrity of security-based swaps entered on or through the facilities of such security-based swap execution facility, including the clearance and settlement of security-based swaps pursuant to section 3C(a)(1) of the Act (15 U.S.C. 78c–3(a)(1)).

(b) Notwithstanding the requirements of § 242.810(b)(2), the rules of a security-based swap execution facility relating to the trading on the security-based swap execution facility, of

security-based swaps that will not be cleared at a registered clearing agency may permit a participant to take into account counterparty credit risk.

§ 242.816 Emergency authority.

(a) A security-based swap execution facility shall establish rules and procedures to provide for the exercise of emergency authority, in consultation or cooperation with the Commission, as necessary or appropriate, which rules and procedures shall include the items set forth in paragraphs (b) and (c) of this section.

(b) A security-based swap execution facility shall establish rules and procedures that specify:

(1) The person or persons authorized by the security-based swap execution facility to declare an emergency;

(2) How the security-based swap execution facility will notify the Commission of its decision to exercise its emergency authority;

(3) How the security-based swap execution facility will notify the public of its decision to exercise its emergency authority;

(4) The processes for decision-making by the security-based swap execution facility personnel with respect to the exercise of emergency authority, including alternate lines of communication and guidelines to avoid conflicts of interest in the exercise of such authority; and

(5) The processes for determining that an emergency no longer exists and notifying the Commission and the public of such decision.

(c) A security-based swap execution facility shall have rules permitting the security-based swap execution facility to immediately take any or all of the following actions during an emergency:

(1) Impose or modify trading limits, price limits, position limits, or other market restrictions, including suspending or curtailing trading on its market in any security-based swap or class of security-based swaps;

(2) Extend or shorten trading hours;

(3) Coordinate trading halts with markets trading a security or securities underlying any security-based swap;

(4) Coordinate with a registered clearing agency to liquidate or transfer positions in any open security-based swap of one of its participants; and

(5) Any action, if so directed by the Commission.

(d)(1) A security-based swap execution facility shall promptly notify the Commission of the exercise of its emergency authority, followed by submission of written documentation within two weeks following cessation of the emergency explaining the basis for declaring an emergency, how conflicts of interest were minimized, and the extent to which the security-based swap execution facility considered the effect of its emergency action on the markets for the security-based swap and any security or securities underlying the security-based swap;

(2) If a security-based swap execution facility implements any rule or rule amendment in the exercise of its emergency authority, it shall file such rule or rule amendment with the Commission pursuant to § 242.806 prior to the implementation of such rule or rule amendment or, if not practicable, within 24 hours after implementation of such rule or rule amendment.

§ 242.817 Timely publication of trading information.

(a) A security-based swap execution facility shall:

(1) Have the capacity to electronically capture, transmit, and disseminate information on price, trading volume, and other trading data on all security-based swaps executed on or through the security-based swap execution facility; and

(2) Make public timely information on price, trading volume, and other trading data on security-based swaps to the extent and in the manner prescribed by the Commission.

(b) If any security-based swap execution facility makes available information regarding a security-based swap transaction to any party other than a counterparty to the transaction, then the security-based swap execution facility must make that information available to all participants on terms and conditions that are fair and reasonable and not unfairly discriminatory; provided however, that nothing in this paragraph shall prohibit a security-based swap execution facility from acting as the agent of a reporting party, as defined in § 242.900 ( ), for purposes of reporting required information directly to a registered security-based swap data repository.

(c) A security-based swap execution facility shall not make any information regarding a security-based swap transaction publicly available prior to the time a security-based swap data repository is permitted to publicly disseminate such information under § 242.902.

§ 242.818 Recordkeeping and reporting.

(a) A security-based swap execution facility shall keep and preserve at least one copy of all documents, including all correspondence, memoranda, papers, books, notices, accounts, and other such records (including the audit trail records required pursuant to the provisions of paragraph (c) of this section) as shall be made or received by it in the conduct of its business.

(b) A security-based swap execution facility shall keep and preserve all such documents and other records for a period of not less than five years, the first two years in an easily accessible place.

(c) A security-based swap execution facility shall establish and maintain accurate, time-sequenced records of all orders, requests for quotations, responses, quotations, other trading interest, and transactions that are received by, originated on, or executed on the security-based swap execution facility. These records shall include the key terms of each order, request for quotation, response, quotation, other trading interest, or transaction and shall document the complete life of each order, request for quotation, response, quotation, other trading interest, or transaction on the security-based swap execution facility, including any modification, cancellation, execution, or any other action taken with respect to such order, request for quotation, response, quotation, other trading interest, or transaction.

(d) A security-based swap execution facility shall establish, maintain, and enforce written policies and procedures to verify the accuracy of the transaction data that it collects and reports.

(e) A security-based swap execution facility shall report to the Commission, in a form and manner acceptable to the Commission, such information as the Commission may, from time to time, determine to be necessary to perform the duties of the Commission under the Act.

(f) A security-based swap execution facility shall, upon request of any representative of the Commission, promptly furnish to the possession of such representative copies of any documents, in such form and manner acceptable to such representative, required to be kept and preserved by it pursuant to paragraphs (a) and (b) of this section.

§ 242.819 Antitrust considerations.

Unless necessary or appropriate to achieve compliance with the Act and the rules and regulations thereunder, a security-based swap execution facility shall not:

(a) Adopt any rule or take any action that results in any unreasonable restraint of trade; or

(b) Impose any material anticompetitive burden on trading or clearing.

§ 242.820 Conflicts of interest.

For additional rules relating to the mitigation of conflicts of interest of security-based swap execution facilities, *see* § 242.702.

(a) The rules of a security-based swap execution facility shall assure a fair representation of its participants in the selection of its directors and administration of its affairs, but no less than 20 percent of the total number of directors of the security-based swap execution facility must be selected by the participants; provided, however, that the security-based swap execution facility shall preclude any participant, or any group or class of participants, either alone or together with its related persons, that beneficially owns, directly or indirectly, an interest in the security-based swap execution facility from dominating or exercising disproportionate influence in the selection of such directors if the participant may thereby dominate or exercise disproportionate influence in the selection or appointment of the entire Board.

(b) At least one director on the Board shall be representative of investors who are not security-based swap dealers or major security-based swap participants, and such director must not be a person associated with a participant.

(c) The rules of a security-based swap execution facility must establish a fair process for participants to nominate an alternative candidate or candidates to the Board by petition and shall specify the percentage of the participants that is necessary to put forth such alternative candidate or candidates, which percentage shall not be unreasonable.

§ 242.821 Financial resources.

(a) A security-based swap execution facility shall have adequate financial, operational, and managerial resources to discharge each responsibility of the security-based swap execution facility, as determined by the Commission.

(b) The financial resources of a security-based swap execution facility shall be considered to be adequate if, when using reasonable estimates and assumptions and not overestimating resources or underestimating expenses, liabilities, and financial exposure, the value of the financial resources:

(1) Enables the security-based swap execution facility to meet its financial obligations to participants, notwithstanding a default by the participant creating the largest financial exposure for the security-based swap execution facility in extreme but plausible market conditions; and

(2) Exceeds the total amount that would enable the security-based swap execution facility to cover its operating costs for a one-year period, as calculated on a rolling basis.

§ 242.822 System safeguards.

(a) *Requirements for security-based swap execution facilities.* A security-based swap execution facility, with respect to those systems that support or are integrally related to the performance of its activities, shall:

(1) Establish, maintain, and enforce written policies and procedures reasonably designed to ensure that its systems provide adequate levels of capacity, resiliency, and security. These policies and procedures shall, at a minimum, require the security-based swap execution facility to:

(i) Establish reasonable current and future capacity estimates, including quantifying in appropriate units of measure the limits of the security-based swap execution facility's capacity to receive (or collect), process, store, or display (or disseminate for display or other use) the data elements included within each function, and identifying the factors (mechanical, electronic, or other) that account for the current limitations;

(ii) Conduct periodic, capacity stress tests of critical systems to determine such systems' ability to process transactions in an accurate, timely, and efficient manner;

(iii) Develop and implement reasonable procedures to review and keep current its system development and testing methodology;

(iv) Review the vulnerability of its systems and data center computer operations to internal and external threats, physical hazards, and natural disasters;

(v) Establish adequate contingency and disaster recovery plans that shall include plans to resume trading of security-based swaps by the security-based swap execution facility no later than the next business day following a wide-scale disruption. In developing such plans, the security-based swap execution facility shall take into account:

(A) The extent of alternative trading venues for the security-based swaps traded by the security-based swap execution facility, including the number of security-based swaps traded on the security-based swap execution facility, the market share of the security-based swap execution facility, and the number of participants on the security-based swap execution facility; and

(B) The necessity of geographic diversity and diversity of infrastructure between the security-based swap execution facility's primary site and any back-up sites.

(2) On an annual basis, submit an objective review to the Commission within 30 calendar days of completion. Where the objective review is performed by an internal department, an objective, external firm shall assess the internal department's objectivity, competency, and work performance with respect to the review performed by the internal department. The external firm must issue a report of the objective review, which the security-based swap execution facility must submit to the Commission on an annual basis, within 30 calendar days of completion of the review;

(3) Promptly notify the Commission in writing of material systems outages and any remedial measures that have been implemented or are contemplated. Prompt notification includes the following:

(i) Immediately notify the Commission when a material systems outage is detected;

(ii) Immediately notify the Commission when remedial measures are selected to address the material systems outage;

(iii) Immediately notify the Commission when the material systems outage is addressed; and

(iv) Submit to the Commission within five business days of when the material systems outage occurred a more detailed written description and analysis of the outage and any remedial measures that have been implemented or are contemplated.

(4) Notify the Commission in writing at least 30 calendar days before implementation of any planned material systems changes.

(b) *Electronic filing.* A security-based swap execution facility shall submit a notification, review, or description and analysis that is required to be submitted to the Commission pursuant to this section in an appropriate electronic format. Any such notification, review, or description and analysis shall be submitted to the Division of Trading and Markets, Office of Market Operations, at the principal office of the Commission in Washington, DC. Any such notification, review, or description and analysis shall be considered submitted when an electronic version is received at the Division of Trading and Markets at the principal office of the Commission in Washington, DC.

(c) *Confidential treatment.* A person who submits a notification, review, or description and analysis pursuant to this section for which such person seeks confidential treatment shall clearly mark each page or segregable portion of

each page with the words "Confidential Treatment Requested." A notification, review, or description and analysis submitted pursuant to this section will be accorded confidential treatment to the extent permitted by law.

§ 242.823 Designation of Chief Compliance Officer of security-based swap execution facility.

(a) *In general.* Each security-based swap execution facility shall identify on Form SB SEF (referenced in § 249.1700 of this chapter) a person who has been designated by the Board to serve as a Chief Compliance Officer of the security-based swap execution facility. The compensation and removal of the Chief Compliance Officer shall require the approval of a majority of the Board.

(b) *Duties.* Each Chief Compliance Officer designated by a registered security-based swap execution facility shall:

(1) Report directly to the Board or the senior officer of the security-based swap execution facility;

(2) Review the compliance of the security-based swap execution facility with the Core Principles described in section 3D of the Act (15 U.S.C. 78c–4) and the rules and regulations thereunder;

(3) In consultation with the Board or the senior officer of the security-based swap execution facility, resolve any conflicts of interest that may arise;

(4) Be responsible for establishing and administering each policy and procedure that is required to be established pursuant to section 3D of the Act (15 U.S.C. 78c–4) and the rules and regulations thereunder;

(5) Monitor compliance with the Act and the rules and regulations thereunder relating to its business as a security-based swap execution facility, including each rule prescribed by the Commission under section 3D of the Act (15 U.S.C. 78c–4);

(6) Establish procedures for the remediation of noncompliance issues identified by the Chief Compliance Officer through any:

(i) Compliance office review;

(ii) Look-back;

(iii) Internal or external audit finding;

(iv) Self-reported error; or

(v) Validated complaint; and

(7) Establish and follow appropriate procedures for the handling, management response, remediation, retesting, and closing of noncompliance issues.

(c) *Annual Reports.* (1) *In general.* The Chief Compliance Officer shall annually prepare and sign a report that contains a description of the compliance of the registered security-based swap execution facility with respect to the Act and the rules and regulations thereunder and each policy and procedure of the security-based swap execution facility (including the code of ethics and conflicts of interest policies of the security-based swap execution facility). Each compliance report shall also contain, at a minimum, a description of:

(i) The security-based swap execution facility's enforcement of its policies and procedures;

(ii) Information on all investigations, inspections, examinations, and disciplinary cases opened, closed, and pending during the reporting period;

(iii) All grants of access (including, for all participants, the reasons for granting such access) and all denials or limitations of access (including, for each applicant, the reasons for denying or limiting access), consistent with § 242.811(b)(3);

(iv) Any material changes to the policies and procedures since the date of the preceding compliance report;

(v) Any recommendation for material changes to the policies and procedures as a result of the annual review, the rationale for such recommendation, and whether such policies and procedures were or will be modified by the security-based swap execution facility to incorporate such recommendation;

(vi) The results of the security-based swap execution facility's surveillance program, including information on the number of reports and alerts generated, and the reports and alerts that were referred for further investigation or for an enforcement proceeding;

(vii) Any complaints received regarding the security-based swap execution facility's surveillance program; and

(viii) Any material compliance matters identified since the date of the preceding compliance report.

(2) *Requirements.* A financial report of the security-based swap execution facility shall be filed with the Commission as described in paragraph (e) of this section and shall accompany a compliance report as described in paragraph (c)(1) of this section. The compliance report shall include a certification that, under penalty of law, the compliance report is accurate and complete. The compliance report shall also be filed in a tagged data format in accordance with the instructions contained in the EDGAR Filer Manual, as described in § 232.301 of this chapter.

(d) The Chief Compliance Officer shall submit the annual compliance report to the Board for its review prior to the submission of the report to the Commission.

(e) *Financial report.* With each annual compliance report, the Chief Compliance Officer shall also prepare and submit to the Commission a financial report of the security-based swap execution facility. Each financial report filed with a compliance report shall:

(1) For the financial statements relating to the security-based swap execution facility:

(i) Be a complete set of financial statements of the security-based swap execution facility that are prepared in accordance with U.S. generally accepted accounting principles for the two most recent fiscal years of the security-based swap execution facility;

(ii) Be audited in accordance with standards of the Public Company Accounting Oversight Board by a registered public accounting firm that is qualified and independent in accordance with § 210.2–01 of this chapter;

(iii) Include a report of the registered public accounting firm that complies with paragraphs (a) through (d) of § 210.2–02 of this chapter;

(iv) Include the accounting policies and practices of the security-based swap execution facility; and

(v) If the security-based swap execution facility's financial statements contain consolidated information of the security-based swap execution facility's subsidiaries, then the security-based swap execution facility's financial statement must provide condensed financial information, in a financial statement footnote, as to the financial position, changes in financial position, and results of operations of the security-based swap execution facility, as of the same dates and for the same periods for which audited consolidated financial statements are required. Such financial information need not be presented in greater detail than is required for condensed statements by § 210.10–01(a)(2), (3), and (4) of this chapter. Detailed footnote disclosure that would normally be included with complete financial statements may be omitted with the exception of disclosures regarding material contingencies, long-term obligations, and guarantees. Descriptions of significant provisions of the security-based swap execution facility's long-term obligations, mandatory dividend or redemption requirements of redeemable stocks, and guarantees of the security-based swap execution facility shall be provided along with a five-year schedule of maturities of debt. If the material contingencies, long-term obligations, redeemable stock requirements, and guarantees of the security-based swap

execution facility have been separately disclosed in the consolidated statements, then they need not be repeated in this schedule.

(2) For the financial statements of a security-based swap execution facility's affiliated entities (any subsidiary in which the applicant has, directly or indirectly, a 25% interest and for any entity that has, directly or indirectly, a 25% interest in the applicant):

(i) Be a complete set of unconsolidated financial statements (in English) for the latest two fiscal years; and

(ii) Include such footnotes and other disclosures as are necessary to avoid rendering the financial statements misleading.

(3) All financial statements must be provided in eXtensible Business Reporting Language consistent with § 232.405 (a)(1), (a)(3), (b), (c), (d), and (e) of this chapter; and

(4) If the financial report required by § 242.823(e) is submitted to the Commission on Form SB SEF (referenced in § 249.1700 of this chapter) pursuant to § 242.802(f) at the same time that the Chief Compliance Officer submits the annual compliance report required by § 242.823(c) and the Chief Compliance Officer represents in the annual compliance report that the financial report has been submitted on Form SB SEF pursuant to § 242.802(f), the Chief Compliance Officer need not also submit the financial report as part of the annual compliance report.

(f) Reports filed pursuant to paragraphs (c) and (e) of this section shall be filed within 60 days after the end of the fiscal year covered by such reports.

PART 249—FORMS, SECURITIES EXCHANGE ACT OF 1934

7. The general authority citation for Part 249 continues to read in part as follows:

Authority: 15 U.S.C. 78a *et seq.* and 7201 *et seq.;* and 18 U.S.C. 1350 unless otherwise noted.

Subpart O—[Removed and reserved]

8. Remove and reserve Subpart O to Part 249.

9. Add Subpart R (consisting of § 249.1700) to Part 249 to read as follows:

Subpart R—Forms for Security-Based Swap Execution Facilities

§ 249.1700 Form SB SEF, form for application for registration as a security-based swap execution facility and for amendments to the registration form of a registered security-based swap execution facility.

Note: Form SB SEF does not appear in the Code of Federal Regulations.

FORM SB SEF

APPLICATION FOR, AND AMENDMENTS TO APPLICATION FOR, REGISTRATION AS A SECURITY-BASED SWAP EXECUTION FACILITY

FORM SB SEF INSTRUCTIONS

A. GENERAL INSTRUCTIONS

1. Form SB SEF (referenced in 17 CFR 249.1700) is the form for the application for, and amendment to application for, registration as a security-based swap execution facility ("SB SEF") pursuant to Section 3D of the Securities Exchange Act of 1934 (15 U.S.C. 78c–4) ("Exchange Act") and the rules of Regulation SB SEF thereunder.
2. **UPDATING**—An applicant or registered SB SEF must file amendments to its Form SB SEF in accordance with 17 CFR 242.802 and 804, as applicable.
3. **CONTACT EMPLOYEE**—The individual listed on the Execution Page (Page 1) of this Form SB SEF as the contact employee must be authorized to receive all contact information, communications, and mailings, and is responsible for disseminating such information within the applicant's organization.
4. **FORMAT**
   - Attach an Execution Page (Page 1) with original manual signatures.
   - Please type all information.
   - Use only the current version of this Form SB SEF or a reproduction.
5. If the information called for by any Exhibit is available in printed form, the printed material may be filed, provided it does not exceed 8½ x 11 inches in size.
6. If any Exhibit required is inapplicable, a statement to that effect shall be furnished in lieu of such Exhibit.
7. A SB SEF that is filing this Form SB SEF as an application may not satisfy the requirements to provide certain information by means of an Internet web page. However, all materials must be filed with the Securities and Exchange Commission ("SEC" or "Commission") electronically, unless the Commission requests that the materials be filed in paper.
8. **WHERE TO FILE AND NUMBER OF COPIES**—Submit one original and two copies of this Form SB SEF to: SEC, Division of Trading and Markets, Office of Market Supervision, 100 F Street, N.E., Washington, DC 20549–7010.
9. **PAPERWORK REDUCTION ACT DISCLOSURE**
   - This Form SB SEF requires an applicant seeking to register as a SB SEF to provide the Commission with certain information regarding the operation of the SB SEF.
   - §§ 242.802 and 242.804 also require registered SB SEFs to update certain information on this Form SB SEF on a periodic basis and the entire Form SB SEF annually.
   - 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 control number. Sections 3(a)(77), 3C(h), 3D(a), 3D(d), 3D(e), 3D(f) and 23(a) of the Exchange Act authorize the Commission to collect information on this Form SB SEF from SB SEFs. See 15 U.S.C. §§ 78c(a)(77), 78e, 78c–4(h), 78c–4(a), 78c–4(d), 78c–4(e), 78c–4(f) and 78w(a).
   - Any member of the public may direct to the Commission any comments concerning the accuracy of the burden estimate on the facing page of this Form SB SEF and any suggestions for reducing this burden.
   - This Form SB SEF is designed to enable the Commission to determine whether a SB SEF applying for registration is in compliance with the provisions of Section 3D of the Exchange Act (15 U.S.C. 78c–4) and the rules under Regulation SB SEF thereunder.
   - It is estimated that a SB SEF will spend approximately 694 hours and $523,000 completing the initial application on Form SB SEF pursuant to 17 CFR 242.801. It is estimated that each SB SEF controlled by another person and each non-resident SB SEF will spend approximately an additional 1 hour and $900 to complete Exhibit P to the initial application on this Form SB SEF. It is also estimated that each SB SEF will spend approximately 25 hours to prepare each periodic amendment to its Form SB SEF pursuant to 17 CFR 242.802(a) and (b) and approximately 50 hours to prepare each annual update to its Form SB

SEF pursuant to 17 CFR 242.802(f). It is estimated that each SB SEF controlled by another person and each non-resident SB SEF will spend approximately 1 hour and $900 to prepare each amendment to its Form SB SEF pursuant to 17 CFR 242.802(c) and (d), respectively.

- It is mandatory that an applicant seeking to register as a SB SEF file this Form SB SEF with the Commission. It is also mandatory that registered SB SEFs file amendments to this Form SB SEF under 17 CFR 242.802 and 804.
- No assurance of confidentiality is given by the Commission with respect to the responses made in this Form SB SEF. The public has access to the information contained in this Form SB SEF.
- This collection of information has been reviewed by the Office of Management and Budget ("OMB") in accordance with the clearance requirements of 44 U.S.C. § 3507. The applicable Privacy Act system of records is SEC–2 and the routine uses of the records are set forth at 40 FR 39255 (August 27, 1975) and 41 FR 5318 (February 5, 1976).

FORM SB SEF INSTRUCTIONS

B. EXPLANATION OF TERMS

APPLICANT—The entity or organization filing an application for registration as a security-based swap execution facility, or amending any such application, on this Form SB SEF.

AFFILIATE—Shall have the same meaning as set forth in 17 CFR 242.800.

BOARD—Shall have the same meaning as set forth in 17 CFR 242.800.

CONTROL—Shall have the same meaning as set forth in 17 CFR 242.800.

EXCHANGE ACT—The Securities Exchange Act of 1934 (15 U.S.C. 78a *et seq.*).

NON-RESIDENT PERSON—Shall have the same meaning as set forth in 17 CFR 242.800.

PARTICIPANT—Shall have the same meaning as set forth in 17 CFR 242.800.

PERSON—Shall have the same meaning as set forth in section 3(a)(9) of the Exchange Act (15 U.S.C. 78c(a)(9)).

PERSON ASSOCIATED WITH A PARTICIPANT—Shall have the same meaning as set forth in 17 CFR 242.800.

RELATED PERSON—Shall have the same meaning as set forth in 17 CFR 242.800.

SECURITY-BASED SWAP—Shall have the same meaning as set forth in section 3(a)(68) of the Exchange Act (15 U.S.C. 78c(a)(68)) or any rules or regulations thereunder.

SECURITY-BASED SWAP DEALER—Shall have the same meaning as set forth in section 3(a)(71) of the Exchange Act (15 U.S.C. 78c(a)(71)) or any rules or regulations thereunder.

SECURITY-BASED SWAP EXECUTION FACILITY—Shall have the same meaning as set forth in section 3(a)(77) of the Exchange Act (15 U.S.C. 78c(a)(77)) or any rules or regulations thereunder.

REGISTERED SECURITY-BASED SWAP EXECUTION FACILITY—Shall mean any security-based swap execution facility registered pursuant to Section 3D(a) of the Exchange Act (15 U.S.C. 78c–4(a)) and the rules of Regulation SB SEF thereunder.

FORM SB SEF

Execution Page

UNITED STATES SECURITIES AND EXCHANGE COMMISSION WASHINGTON, DC 20549

APPLICATION FOR, AND AMENDMENTS TO APPLICATION FOR, REGISTRATION AS A SECURITY–BASED SWAP EXECUTION FACILITY

WARNING: Failure to keep this form current and to file accurate supplementary information on a timely basis, or the failure to keep accurate books and records or otherwise to comply with the provisions of law applying to the conduct of the applicant, would violate the federal securities laws and may result in disciplinary, administrative, or criminal action.

INTENTIONAL MISSTATEMENTS OR OMISSIONS OF FACTS MAY CONSTITUTE CRIMINAL VIOLATIONS

__APPLICATION FOR REGISTRATION

__ AMENDMENT

If this is an APPLICATION, indicate if the applicant requests consideration for temporary registration pursuant to Rule 801(c) of Regulation SB SEF under the Exchange Act:

____YES

____NO

If this is an AMENDMENT to an application, or to an effective registration (including an annual amendment), list all items that are amended:

_____

_____

1. State the name of the applicant: ____

_____

2. Provide the applicant's primary street address (Do not use a P.O. Box):

_____

(Number and Street)

_____

(City) (State) (Zip Code)

3. Provide the applicant's mailing address (if different):

_____

(Number and Street)

_____

(City) (State) (Zip Code)

4. Provide the applicant's business telephone and facsimile number:

_____

(Telephone) (Facsimile)

5. Provide the name, title, and telephone number of a contact employee:

_____

(Name) (Title) (Telephone)

6. Provide the name and address of counsel for the applicant:

_____

(Name)

_____

(Number and Street)

_____

(City) (State) (Zip Code)

7. Provide the date applicant's fiscal year ends:

_____

8. Indicate legal status of applicant: __ Corporation __ Sole Proprietorship __ Partnership __ Limited Liability Company __ Other (specify):

If other than a sole proprietor, indicate the date and place where the applicant obtained its legal status (e.g. state where incorporated, place where partnership agreement was filed or where the applicant entity was formed), and the statute under which the applicant was organized:

_____

(Date) (MM/DD/YYYY)

_____

State/Country of formation:

_____

(Statute under which the applicant was organized)

9. Applicant understands and consents that any notice or service of process, pleadings, or other documents in connection with any action or proceeding against the applicant may be effectuated by certified mail to the officer specified or person named below at the U.S. address given. Such officer or person cannot be a Commission member, official or employee.

_____

(Name of Person or, if the Applicant is a Corporation, Title of Officer)

_____

(Name of the Applicant or Applicable Entity)

_____

(Number and Street)

_____
(City) (State) (Zip Code)

_____
(Telephone)

EXECUTION: The undersigned, being first duly sworn, deposes and says that he/she has executed this form on behalf of, and with the authority of, said applicant. The undersigned and applicant represent that the information and statements contained herein, including exhibits, schedules, or other documents attached hereto, and other information filed herewith, all of which are made a part hereof, are current, true, and complete. It is understood that all required items and exhibits are considered integral parts of this form and that the submission of any amendment represents that all unamended items and Exhibits remain true, current, and complete as previously filed. The applicant and the undersigned certify that the applicant is currently in compliance with, and is currently operating its business in a manner consistent with, the Exchange Act and all rules and regulations thereunder. The applicant and the undersigned certify that the applicant is so organized, and has the capacity, to assure the prompt, accurate, and reliable performance of its functions as a security-based swap execution facility. The applicant and the undersigned certify that the applicant has the capacity to fulfill its obligations under all international information-sharing agreements to which it is a party. If the applicant is controlled by another person, the applicant and the undersigned certify that any person that controls the applicant has consented to and can, as a matter of law, (i) provide the Commission with prompt access to its books and records, to the extent such books and records are related to the activities of the security-based swap execution facility; and (ii) submit to onsite inspection and examination by representatives of the Commission with respect to the activities of the security-based swap execution facility. If the applicant is a non-resident person, the applicant and the undersigned further represent that the applicant can, as a matter of law, (i) provide the Commission with prompt access to the applicant's books and records and (ii) submit to an onsite inspection and examination by representatives of the Commission.

Date:

_____
(MM/DD/YY)

_____
(Name of applicant)

By:
(Signature)

_____
(Printed Name and Title)

Subscribed and sworn before me this

_____
day of

_____,
(Month)

_____
(Year)

by

_____
(Notary Public)

My Commission expires _____
County of _____
State of _____

This page must always be completed in full with original, manual signature and notarization. Affix notary stamp or seal where applicable.

FORM SB SEF

UNITED STATES SECURITIES AND EXCHANGE COMMISSION WASHINGTON, DC 20549

APPLICATION FOR, AND AMENDMENTS TO APPLICATION FOR, REGISTRATION AS A SECURITY–BASED SWAP EXECUTION FACILITY PURSUANT TO SECTION 3D OF THE EXCHANGE ACT

DO NOT WRITE BELOW THIS LINE—FOR OFFICIAL USE ONLY

EXHIBITS

File all Exhibits with an application for registration as a security-based swap execution facility pursuant to Section 3D of the Exchange Act and Rule 801 of Regulation SB SEF thereunder, or with amendments to such applications pursuant to Rule 802 and 804 of Regulation SB SEF. For each exhibit, include the name of the applicant, the date upon which the exhibit was filed, and the date as of which the information is accurate (if different from the date of the filing). If any Exhibit required is inapplicable, a statement to that effect shall be furnished in lieu of such Exhibit.

Exhibit A A copy of the governing documents of the applicant, including but not limited to, a corporate charter, articles of incorporation or association, limited liability company agreement, or partnership agreement, with all subsequent amendments, and by-laws or corresponding rules or instruments, whatever the name, of the applicant.

Exhibit B A copy of all written rulings, settled practices having the effect of rules, stated policies, and interpretations of the Board or other committee of the applicant in respect of any provisions of the governing documents, rules, or trading practices of the applicant which are not included in Exhibit A.

Exhibit C A list of the officers and directors, or persons performing similar functions who presently hold or have held their offices or positions during the previous year, and a list of all standing committees and their members (including the nominating committee, regulatory oversight committee, and all committees that have the authority to act on behalf of the Board or the nominating committee), indicating the following for each:

1. Name;
2. Title;
3. Dates of commencement and termination of term of office or position;
4. Type of business in which each is primarily engaged (e.g., security-based swap dealer, major security-based swap participant, inter-dealer broker, end-user, etc.);
5. If a director, whether such person qualifies as an "independent director" pursuant to Rule 800 of Regulation SB SEF; and
6. If a director, whether such person is a member of any standing committees, committees that have the authority to act on behalf of the Board, or the nominating committee.

Exhibit D A chart or charts illustrating fully the internal organizational structure of the applicant. The chart or charts should indicate the internal divisions or departments; the responsibilities of each such division or department; and the reporting structure of each division or department, including its oversight by committees (or their equivalent).

Exhibit E A list of all persons that have either, direct or indirect, ownership or voting interest in the security based swap execution facility that equals or exceeds 5% and a list of all related persons of such persons; provided that a related person (1) has ownership or voting interest in the security-based swap execution facility; or (2) is a participant. For each of the persons and related persons listed in this Exhibit E, please provide the following:

1. Full legal name;

2. Title or legal status;
3. Whether such person or related person is a participant;
4. Date that title, legal status, or participation in a security-based swap execution facility was acquired or commenced;
5. Percentage of ownership interest held;
6. Type of ownership interest held, including whether the ownership interest is "beneficial ownership" as defined in Rule 800 of Regulation SB SEF or is entitled to vote;
7. Percentage of voting interest held; and
8. Type of voting interest held.

Exhibit F For the latest two fiscal years of the applicant, financial statements that shall: (1) Be a complete set of financial statements of the applicant that are prepared in accordance with U.S. generally accepted accounting principles for the most recent fiscal year of the applicant; (2) be audited in accordance with standards of the Public Company Accounting Oversight Board by a registered public accounting firm that is qualified and independent in accordance with Rule 2–01 of Regulation S–X (17 CFR 210.2–01); (3) include a report of the registered public accounting firm that complies with paragraphs (a) through (d) of Rule 2–02 of Regulation S–X (17 CFR 210.2–02); (4) include the accounting policies and practices of the applicant; (4) if the applicant's financial statements contain consolidated information of a subsidiary of the applicant, then the applicant's financial statement must provide condensed financial information, in a financial statement footnote, as to the financial position, changes in financial position, and results of operations of the applicant, as of the same dates and for the same periods for which audited consolidated financial statements are required. Such financial information need not be presented in greater detail than is required for condensed statements by Rules 10–01(a)(2), (3), and (4) of Regulation S–X (17 CFR 210.10–01). Detailed footnote disclosure that would normally be included with complete financial statements may be omitted with the exception of disclosures regarding material contingencies, long-term obligations, and guarantees. Descriptions of significant provisions of the applicant's long-term obligations, mandatory dividend or redemption requirements of redeemable stocks, and guarantees of the applicant shall be provided along with a five-year schedule of maturities of debt. If the material contingencies, long-term obligations, redeemable stock requirements, and guarantees of the applicant have been separately disclosed in the consolidated statements, then they need not be repeated in this schedule; and (5) be provided in eXtensible Business Reporting Language consistent with Rules 405 (a)(1), (a)(3), (b), (c), (d), and (e) of Regulation S–T (17 CFR 232.11).

Exhibit G An executed or executable copy of any agreements or contracts entered into or to be entered into by the applicant, or a subsidiary or an affiliate of the applicant, including partnership or limited liability company, third-party regulatory service, or other agreements relating to the operation of an electronic trading system to be used to effect transactions on the security-based swap execution facility ("System"), that enable or empower the applicant to comply with Section 3D of the Exchange Act (15 U.S.C. 78c–4).

Exhibit H For each of the applicant's affiliated entities (every subsidiary in which the applicant has, directly or indirectly, a 25% interest and for every entity that has, directly or indirectly, a 25% interest in the applicant) provide a complete set of unconsolidated financial statements (in English) for the latest two fiscal years and include such footnotes and other disclosures as are necessary to avoid rendering the financial statements misleading. The financial statements shall be provided in eXtensible Business Reporting Language consistent with Rules 405 (a)(1), (a)(3), (b), (c), (d), and (e) of Regulation S–T (17 CFR 232.11). In addition to the foregoing, for all other affiliates of the applicant not listed in the paragraph above, the information required by the paragraph above shall be made available upon request.

Exhibit I Describe the manner of operation of the System. This description should include the following:

1. A detailed description of the manner in which the System satisfies the definition of "security-based swap execution facility" in Section 3(a)(77) of the Exchange Act and any Commission rules, interpretations, or guidelines regarding such definition, including a description of how the System displays all orders, quotes, requests for quote, responses, and trades in an electronic or other form, and the timelines in which the System does so; how orders interact on the System, the ability of market participants to see and transact with orders, quotes, requests for quotes, and responses; and an explanation of the trade-matching algorithm if it is based on order priority factors other than price and time;
2. The means of access to the System, including any limitations on access;
3. Procedures governing entry and display of quotations and orders in the System;
4. Procedures governing the execution, reporting, clearance and settlement of transactions in connection with the System;
5. Proposed fees;
6. Procedures for ensuring compliance with System usage guidelines and rules;
7. The hours of operation of the System and the date on which the applicant intends to commence operation of the System;
8. A copy of the users' manual or equivalent document;
9. If the applicant proposes to hold funds or securities on a regular basis, describe the controls that will be implemented to ensure safety of those funds or securities; and
10. The name of any entity, other than the security-based swap execution facility, that will be involved in operation of the System, including the execution, trading, clearing and settling of transactions on behalf of the security-based swap execution facility, and a description of the role and responsibilities of each entity.

Exhibit J A complete set of all forms pertaining to:

1. Application for participation or use of the security-based swap execution facility.
2. Application for approval as a person associated with a participant or other user of the security-based swap execution facility.
3. Any other similar materials.

Provide a table of contents listing the forms included in this Exhibit J.

Exhibit K A complete set of all forms of financial statements, reports, or questionnaires required of participants or any other users of the security-based swap execution facility relating to financial responsibility or minimum capital requirements for such participants or any other users. Provide a table

of contents listing the forms included in this Exhibit K.

Exhibit L Describe the applicant's criteria for participation in or use of the security-based swap execution facility. Provide a list of all grants of access (including, for all participants, the reasons for granting such access) and all denials or limitations of access (including, for each applicant or participant, the reasons for denying or limiting access). Describe conditions under which participants or persons associated with participants may be subject to suspension or termination with regard to access to the security-based swap execution facility. Describe any procedures that will be involved in the suspension or termination of a participant or person associated with a participant. Provide a list of all disciplinary actions taken.

Exhibit M Provide an alphabetical list of all participants or other users of the security-based swap execution facility, including the following information:

1. Name;
2. Date of acceptance as a participant or other user;
3. Principal business address and telephone number;
4. If participant or other user is an individual, the name of the entity with which such individual is associated and the relationship of such individual to the entity (*e.g.,* partner, officer, director, employee, etc.);
5. Describe the type of activities primarily engaged in by the participant or other user (*e.g.,* security-based swap dealer, major security-based swap participant, inter-dealer broker, other market maker, non-broker dealer, non-security-based swap dealer, commercial end-user, inactive or other functions). A person shall be "primarily engaged" in an activity or function for purposes of this item when that activity or function is the one in which that person is engaged for the majority of their time. When more than one type of person at an entity engages in any of the types of activities or functions enumerated in this item, identify each and state the number of participants, or other users in each; and
6. The class of participation or other access.

Exhibit N Provide a brief description of the criteria used to determine what securities may be traded on the security-based swap execution facility.

Exhibit O Provide a schedule of the security-based swaps to be traded on the security-based swap execution facility, including for each a description of the security-based swap.

Exhibit P (1) If the applicant is controlled by another person, provide an opinion of counsel that any person that controls the applicant has consented to and can, as a matter of law, (i) provide the Commission with prompt access to its books and records, to the extent such books and records are related to the activities of the security-based swap execution facility; and (ii) submit to onsite inspection and examination by representatives of the Commission with respect to the activities of the security-based swap execution facility.

(2) If the applicant is a non-resident person, provide an opinion of counsel that the applicant can, as a matter of law, (i) provide the Commission with prompt access to the books and records of such applicant and (ii) submit to onsite inspection and examination by representatives of the Commission.

By the Commission.

Dated: February 2, 2011.

Elizabeth M. Murphy,

Secretary.

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