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Exemption of Certain Foreign Brokers or Dealers; Proposed Rule

SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 240

[Release No. 34–58047; File No. S7–16–08]

RIN 3235–AK15

Exemption of Certain Foreign Brokers or Dealers

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule.

SUMMARY: The Securities and Exchange Commission (''Commission'' or ''SEC'') is proposing to amend a rule under the Securities Exchange Act of 1934 (''Exchange Act''), which provides conditional exemptions from broker-dealer registration for foreign entities engaged in certain activities involving certain U.S. investors. To reflect increasing internationalization in securities markets and advancements in technology and communication services, the proposed amendments would update and expand the scope of certain exemptions for foreign entities, consistent with the Commission's mission to protect investors, maintain fair, orderly and efficient markets and facilitate capital formation.

DATES: Comments should be received on or before September 8, 2008.

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 S7–16–08 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 Secretary, Securities and Exchange Commission, 100 F Street, NE., Washington, DC 20549–1090.

All submissions should refer to File Number S7–16–08. 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. We will post all comments on the Commission's Internet Web site (*http://www.sec.gov/rules/proposed.shtml*). Comments are also available for public inspection and copying in the Commission's Public Reference Room, 100 F Street, 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; we do not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

FOR FURTHER INFORMATION CONTACT: Erik R. Sirri, Director, Marlon Quintanilla Paz, Senior Counsel to the Director, Brian A. Bussey, Assistant Chief Counsel, Matthew A. Daigler, Special Counsel, or Max Welsh, Attorney, Office of the Chief Counsel, Division of Trading and Markets, at (202) 551–5500, at the Securities and Exchange Commission, 100 F Street, NE., Washington, DC 20549–6628.

SUPPLEMENTARY INFORMATION: The Commission is requesting public comment on the proposed amendments to Rule 15a–6 [17 CFR 240.15a–6] under the Exchange Act.

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I. Introduction and Background

Section 15(a) of the Exchange Act 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.[1] The Commission uses a territorial approach in applying the broker-dealer registration requirements to the international operations of broker-dealers.[2] Under this approach, broker-dealers located outside the United States that induce or attempt to induce securities transactions with persons in the United States are required to register with the Commission, unless an exemption applies.[3] Entities that conduct such activities entirely outside the United States do not have to register. Because this territorial approach applies on an entity level, not a branch level, if a foreign broker-dealer establishes a branch in the United States, broker-dealer registration requirements would extend to the entire foreign broker-dealer entity.[4] The registration requirements do not apply, however, to a foreign broker-dealer with an affiliate, such as a subsidiary, operating in the United States.[5] Only the U.S. affiliate must register and only the U.S. affiliate may engage in securities transactions and perform related functions on behalf of U.S. investors.[6] The territorial approach also requires registration of foreign broker-dealers operating outside the United States that effect, induce or attempt to induce securities transactions for any person inside the United States, other than a foreign person temporarily within the United States.[7]

In response to numerous inquiries seeking no-action relief and interpretive advice regarding whether certain international securities activities required U.S. broker-dealer registration, the Commission issued a release on June 14, 1988, to clarify the registration

[1] *See* 15 U.S.C. 78o(a)(1). Section 3(a)(4) of the Exchange Act generally defines a ''broker'' as ''any person engaged in the business of effecting transactions in securities for the account of others,'' but provides 11 exceptions for certain bank securities activities. Section 3(a)(5) of the Exchange Act generally defines a ''dealer'' as ''any person engaged in the business of buying and selling securities for his own account,'' but includes exceptions for certain bank activities. 15 U.S.C. 78c(a)(4). Exchange Act Section 3(a)(6) defines a ''bank'' as a bank or savings association that is directly supervised and examined by state or federal banking authorities (with certain additional requirements for banks and savings associations that are not chartered by a federal authority or a member of the Federal Reserve System). 15 U.S.C. 78c(a)(6). Accordingly, foreign banks that act as brokers or dealers within the jurisdiction of the United States are subject to U.S. broker-dealer registration requirements. *See* Exchange Act Release No. 27017 (Jul. 11, 1989), 54 FR 30013, 30015 n.16 (Jul. 18, 1989) (''1989 Adopting Release''); and Exchange Act Release No. 25801 (Jun. 14, 1988), 53 FR 23645 at n.1 (Jun. 23, 1988) (''1988 Proposing Release''). To the extent, however, that a foreign bank establishes a branch or agency in the United States that is supervised and examined by a federal or state banking authority and otherwise meets the requirements of Section 3(a)(6), the Commission considers that branch or agency to be a ''bank'' for purposes of the exceptions from the ''broker'' and ''dealer'' definitions. *See* 1989 Adopting Release, 54 FR at 30015 n.16.

[2] *See* 1989 Adopting Release, 54 FR at 30016.

[3] *See id.*

[4] *See id.* at 30017.

[5] *See id.*

[6] *See id.*

[7] *See id.* For contacts by foreign broker-dealers with U.S. citizens domiciled abroad, the Commission generally does not require registration. Paragraph (a)(4)(v) of Rule 15a–6 specifically addresses this situation.

requirements for foreign-based broker-dealers, foreign affiliates of U.S. broker-dealers, and other foreign financial institutions.[8] The release also proposed Rule 15a–6, which provided conditional exemptions from registration under Section 15(b) of the Exchange Act for foreign broker-dealers that induce or attempt to induce the purchase or sale of any security by certain U.S. institutional investors, if the foreign broker-dealer satisfied certain conditions. The Commission adopted Rule 15a–6 on July 11, 1989, and it became effective August 15, 1989.[9]

While the rule has provided a useful framework for certain U.S. investors to access foreign broker-dealers for almost two decades, ever increasing market globalization suggests that it is time to revisit that framework to consider whether it could be made more workable, consistent with the Commission's mission to protect investors, maintain fair, orderly and efficient markets and facilitate capital formation.

As discussed below, the amendments we propose today would generally expand the category of U.S. investors that foreign broker-dealers may contact for the purpose of providing research reports and soliciting securities transactions. The proposed amendments would also reduce the role U.S. registered broker-dealers must play in intermediating transactions effected by foreign broker-dealers on behalf of certain U.S. investors. Proposed new safeguards are intended to ensure that the expanded exemptions would remain consistent with the Commission's statutory mandate.

II. The Regulatory Framework Under Rule 15a–6

As discussed below, Rule 15a–6 provides conditional exemptions from broker-dealer registration for foreign broker-dealers that engage in certain activities involving certain U.S. investors. Paragraph (b)(3) of the rule defines a ''foreign broker-dealer'' as ''any non-U.S. resident person * * * that is not an office or branch of, or a natural person associated with, a registered broker-dealer, whose securities activities, if conducted in the United States, would be described by the definition of 'broker' or 'dealer' in Section 3(a)(4) or 3(a)(5) of the Act.'' [10] Among the activities that foreign broker-dealers may engage in under the rule are: (i) ''Nondirect'' contacts by foreign broker-dealers with U.S. investors through execution of unsolicited securities transactions and the provision of research reports to certain U.S. institutional investors and (ii) ''direct'' contacts, involving the execution of transactions through a registered broker-dealer intermediary with or for certain U.S. institutional investors, and without this intermediary with or for certain entities such as registered broker-dealers and banks acting in a broker or dealer capacity.[11]

A. Unsolicited Trades

As we explained in adopting Rule 15a–6, a broker-dealer that solicits a transaction with a U.S. investor must be registered with the Commission.[12] Because the Commission determined that, as a policy matter, registration is not necessary if a U.S. investor initiated a transaction with a foreign broker-dealer entirely by his or her own accord, paragraph (a)(1) of Rule 15a–6 [13] provides an exemption for a foreign-broker dealer that effects unsolicited securities transactions with U.S. persons.[14] As the Commission expressed in adopting Rule 15a–6, solicitation is construed broadly as ''any affirmative effort by a broker or dealer intended to induce transactional business for the broker-dealer or its affiliates.'' [15] For example, the Commission views telephone calls to U.S. investors, advertising circulated or broadcast in the United States and holding investment seminars in the United States, regardless of whether the seminars were hosted by a registered broker-dealer, as forms of solicitation.[16] Solicitation also includes recommending the purchase or sale of securities to customers or prospective customers for the purpose of generating transactions.[17]

The exemption in paragraph (a)(1) is intended to allow a foreign broker-dealer to effect transactions with U.S. investors when the foreign broker-dealer does not make any affirmative effort to induce transactional activity with the U.S. investor. Because of the breadth of the meaning of solicitation in the broker-dealer registration context, this exemption typically would not be a viable basis for a foreign broker-dealer to conduct an ongoing business, which would likely involve some form of solicitation, in the United States.[18]

B. Provision of Research Reports

The provision of research to investors also may constitute solicitation by a broker or dealer that would require broker-dealer registration.[19] Broker-dealers often provide research to customers with the expectation that the customer eventually will trade through the broker-dealer.[20] Paragraph (a)(2) of Rule 15a–6 [21] provides an exemption from U.S. broker-dealer registration for foreign broker-dealers that provide research reports to certain institutional investors under conditions that are designed to permit the flow of research without allowing foreign broker-dealers to do more to solicit transactions with U.S. investors.[22]

In particular, the rule exempts from U.S. broker-dealer registration a foreign broker-dealer that provides research to certain U.S. institutional investors if (i) the research reports do not recommend that the investor use the foreign broker-dealer to effect trades in any security, (ii) the foreign broker-dealer does not initiate follow up contacts or otherwise induce or attempt to induce investors to effect transactions in any security, (iii) transactions with the foreign broker-dealer in securities covered by the research reports are effected through a registered broker-dealer according to the provisions of paragraph (a)(3) of the rule, described below, and (iv) the provision of research is not pursuant to an understanding that the foreign broker-dealer will receive commission income from transactions effected by U.S. investors.[23]

The exemption in paragraph (a)(2) of Rule 15a–6 is available only with

[8] *See* 1988 Proposing Release.

[9] 17 CFR 240.15a–6. *See* 1989 Adopting Release.

[10] 17 CFR 240.15a–6(b)(3).

[11] *See* 1989 Adopting Release, 54 FR at 30013.

[12] *See id.* at 30017.

[13] 17 CFR 240.15a–6(a)(1).

[14] *See* 1989 Adopting Release, 54 FR at 30017.

[15] *See id.*

[16] *See id.* at 30017–18.

[17] *See id.*

[18] *See id.*; *see also* Exchange Act Release No. 39779, ''Interpretation Re: Use of Internet Web Sites To Offer Securities, Solicit Securities Transactions, or Advertise Investment Services Offshore'' (Mar. 23, 1998), 63 FR 14806, 14813 (Mar. 27, 1998) (stating that ''[f]oreign broker-dealers that have Internet Web sites and that intend to rely on Rule 15a–6's 'unsolicited' exemption should ensure that the 'unsolicited' customer's transactions are not in fact solicited, either directly or indirectly, through customers accessing their Web sites.'').

[19] *See* 1989 Adopting Release, 54 FR at 30021–22.

[20] *See id.* (''Broker-dealers often provide research to customers on a non-fee basis, with the expectation that the customer eventually will trade through the broker-dealer. They may provide research to acquaint potential customers with their existence, to maintain customer goodwill, or to inform customers of their knowledge of specific companies or markets, so that these customers will be encouraged to use their execution services for that company or those markets. In each instance, the basic purpose of providing the non-fee research is to generate transactional business for the broker-dealer. In the Commission's view, the deliberate transmission of information, opinions, or recommendations to investors in the United States, whether directed at individuals or groups, could result in the conclusion that the foreign broker-dealer has solicited those investors.'').

[21] 17 CFR 240.15a–6(a)(2).

[22] *See* 17 CFR 240.15a–6(a)(2).

[23] *See id.*

respect to research reports that are furnished to ''major U.S. institutional investors.'' Paragraph (b)(4) of the rule defines a ''major U.S. institutional investor'' as (i) a U.S. institutional investor [24] that has, or has under management, total assets in excess of $100 million (which may include the assets of any family of investment companies of which it is a part); or (ii) an investment adviser registered with the Commission under Section 203 of the Investment Advisers Act of 1940 that has total assets under management in excess of $100 million.[25]

C. Solicited Trades

As we discussed in adopting Rule 15a–6, although many foreign broker-dealers have established registered broker-dealer affiliates to deal with U.S. investors and trade in U.S. securities, they may prefer to deal with institutional investors in the United States from their overseas trading desks, where their dealer operations and principal sources of current information on foreign market conditions and foreign securities are based.[26] For similar reasons, many U.S. institutions want direct contact with overseas traders. Except for limited instances of unsolicited transactions, such contact would require the foreign broker-dealer to register with the Commission.

Paragraph (a)(3) of Rule 15a–6 [27] provides an exemption for foreign broker-dealers that induce or attempt to induce securities transactions by certain institutional investors, if a U.S. registered broker-dealer intermediates certain aspects of the transactions by carrying out specified functions. In particular, the U.S. registered broker-dealer is required to effect all aspects of the transaction (other than negotiation of the terms).[28] It must issue all required confirmations [29] and account statements to the U.S. institutional investor or major U.S. institutional investor. As the Commission explained, these documents are significant points of contact between the investor and the broker-dealer, and they provide important information for investors.[30] Also, as between the foreign broker-dealer and the U.S. registered broker-dealer, the latter is required to extend or arrange for the extension of any credit to these investors in connection with the purchase of securities.[31] In addition, the U.S. registered broker-dealer is responsible for maintaining required books and records relating to the transactions conducted under paragraph (a)(3) of the rule, including those required by Rules 17a–3 and 17a–4,[32] which facilitates Commission supervision and investigation of these transactions.[33] Of course, the U.S. registered broker-dealer also must maintain sufficient net capital in compliance with Exchange Act Rule 15c3–1,[34] and receive, deliver and safeguard funds and securities in connection with the transactions in compliance with Exchange Act Rule 15c3–3.[35] Furthermore, the U.S. registered broker-dealer must take responsibility for certain key sales activities, including ''chaperoning'' the contacts of foreign associated persons with certain U.S. institutional investors.[36]

In adopting Rule 15a–6, the Commission pointed out that the U.S. registered broker-dealer's intermediation is intended to help protect U.S. investors and securities markets.[37] For example, the U.S. registered broker-dealer has an obligation, as it has for all customer accounts, to review any Rule 15a–6(a)(3) account for indications of potential problems.[38]

This exemption in Rule 15a–6(a)(3) applies to transactions with major U.S. institutional investors, described above, as well as ''U.S. institutional investors.'' The rule defines a ''U.S. institutional investor'' as (i) an investment company registered with the Commission under Section 8 of the Investment Company Act of 1940; or (ii) a bank, savings and loan association, insurance company, business development company, small business investment company, or employee benefit plan defined in Rule 501(a)(1) of Regulation D under the Securities Act of 1933 (''Securities Act''); a private business development company defined in Rule 501(a)(2); an organization described in Section 501(c)(3) of the Internal Revenue Code, as defined in Rule 501(a)(3); or a trust defined in Rule 501(a)(7).[39]

D. Counterparties and Specific Customers

Paragraph (a)(4) of Rule 15a–6 [40] provides an exemption for foreign broker-dealers that effect transactions in securities with or for, or induce or attempt to induce the purchase or sale of securities by, five categories of persons: (1) Registered broker-dealers (acting either as principal or for the account of others) or banks acting pursuant to an exception or exemption from the definition of ''broker'' or ''dealer'' in Sections 3(a)(4)(B), 3(a)(4)(E), or 3(a)(5)(C) of the Exchange Act or the rules thereunder; [41] (2) certain international organizations and their agencies, affiliates and pension funds; [42]

[24] *See* Part II.C., *infra*, for discussion of the definition of ''U.S. institutional investor.''

[25] *See* 17 CFR 240.15a–6(b)(4); *cf.* Letter from Richard R. Lindsey, Director, Division of Market Regulation, to Mr. Giovanni P. Prezioso, Cleary Gottlieb, Steen & Hamilton (Apr. 9, 1997) (''1997 Staff Letter'').

[26] *See* 1989 Adopting Release, 54 FR at 30024.

[27] 17 CFR 240.15a–6(a)(3).

[28] 17 CFR 240.15a–6(a)(3)(iii)(A). In adopting Rule 15a–6, the Commission recognized that rules of foreign securities exchanges and over-the-counter markets may require the foreign broker-dealer, as a member or market maker, to perform the actual physical execution of transactions in foreign securities listed on those exchanges or traded in those markets. *See* 1989 Adopting Release, 54 FR at 30029 n.185. For this reason, the Commission stated that, while it does not believe that it is appropriate to allow the U.S. registered broker-dealer to delegate the performance of its duties under the rule to the foreign broker-dealer, it would permit such delegation in the case of physically executing foreign securities trades in foreign markets or on foreign exchanges. *See* 1989 Adopting Release, 54 FR at 30025; cf. 1997 Staff Letter. As a result, the treatment of U.S. securities and foreign securities under paragraph (a)(3) of the rule differs. Specifically, with foreign securities the foreign broker-dealer may not only negotiate the terms, but also execute the transactions in the circumstances specified in the Adopting Release. *See* 1989 Adopting Release, 54 FR at 30029 n.185; cf. NASD Rule 6620(g)(2) (trade reporting of transactions in foreign equity securities not required when the transaction is executed on and reported to a foreign securities exchange or over the counter in a foreign country and reported to the foreign regulator). With respect to U.S. securities, however, the U.S. broker-dealer is required to execute the transactions and to comply with the provisions of the federal securities laws, the rules thereunder and SRO rules applicable to the execution of transactions.

[29] *See* Rule 10b–10, 17 CFR 240.10b–10. *See* 17 CFR 240.15a–6(a)(3)(iii)(A)(2).

[30] *See* 1989 Adopting Release, 54 FR at 30029.

[31] 17 CFR 240.15a–6(a)(3)(iii)(A)(3).

[32] 17 CFR 240.17a–3 and 17a–4. *See* 17 CFR 240.15a–6(a)(3)(iii)(A)(4).

[33] *See* 1989 Adopting Release, 54 FR at 30029.

[34] 17 CFR 240.15c3–1. *See* 17 CFR 240.15a–6(a)(3)(iii)(A)(5).

[35] 17 CFR 240.15c3–3. *See* 17 CFR 240.15a–6(a)(3)(iii)(A)(6); cf. 1997 Staff Letter.

[36] *See* 17 CFR 240.15a–6(a)(3)(ii)(A) and (a)(3)(iii)(B); *cf.* 1997 Staff Letter.

[37] *See* 1989 Adopting Release, 54 FR at 30025.

[38] *See id.* While the rule does not require the U.S. registered broker-dealer to implement procedures to obtain positive assurance that the foreign broker-dealer is operating in accordance with U.S. requirements, the U.S. registered broker-dealer, in effecting trades arranged by the foreign broker-dealer, has a responsibility to review these trades for indications of possible violations of the federal securities laws. *Id.*

[39] *See* 17 CFR 240.15a–6(b)(7).

[40] 17 CFR 240.15a–6(a)(4).

[41] While the exemption allows foreign broker-dealers to effect transactions with or for certain banks or registered broker-dealers, it does not allow direct contact by foreign broker-dealers with the U.S. customers of the registered broker-dealers or banks. *See* 1989 Adopting Release, 54 FR at 30013 n.202.

[42] The organizations are the African Development Bank, the Asian Development Bank, the Inter-American Development Bank, the International Bank for Reconstruction and Development, the International Monetary Fund, the United Nations. *See* 17 CFR 240.15a–6(a)(4)(ii).

(3) foreign persons temporarily present in the United States with whom the foreign broker-dealer had a pre-existing relationship; (4) any agency or branch of a U.S. person permanently abroad; and (5) U.S. citizens resident outside the United States, as long as the transactions occur outside the United States and the foreign broker-dealer does not target solicitations at identifiable groups of U.S. citizens resident abroad.

III. Proposed Amendments to Rule 15a–6

The pace of internationalization in securities markets around the world has continued to accelerate since we adopted Rule 15a–6 in 1989. Advancements in technology and communication services have provided greater access to global securities markets for all types of investors.[43] U.S. investors are seeking to take advantage of this increased access by seeking more direct contact with those expert in foreign markets and foreign securities. In addition, discussions over the years with industry representatives regarding Rule 15a–6 have suggested areas where the rule could be revised to achieve its objectives more effectively without jeopardizing investor protections.[44]

In response to these developments and suggestions, the Commission is proposing to amend Rule 15a–6 to remove barriers to access while maintaining key investor protections. In general, and as discussed more fully in Part III.G. below, the proposed amendments would expand and streamline the conditions under which a foreign broker-dealer could operate without triggering the registration requirements of Section 15(a)(1) or 15B(a)(1) of the Exchange Act and the reporting and other requirements of the Exchange Act (other than Sections 15(b)(4) and 15(b)(6)), and the rules and regulations thereunder, that apply specifically to a broker-dealer that is not registered with the Commission solely by virtue of its status as a broker or dealer, while maintaining a regulatory structure designed to protect investors and the public interest.[45]

A. Extension of Rule 15a–6 to Qualified Investors

The proposed rule would expand the category of U.S. investors with which a foreign broker-dealer[46] could interact under Rule 15a–6(a)(2) and would expand, with a few exceptions, the category of U.S. investors with which a foreign broker-dealer could interact under Rule 15a–6(a)(3) by replacing the categories of ''major U.S. institutional investor'' and ''U.S. institutional investor'' with the category of ''qualified investor,'' as defined in Section 3(a)(54) of the Exchange Act.[47] In adopting the definitions of ''U.S. institutional investor'' and ''major U.S. institutional investor,'' the Commission expressed the view that institutions with the major U.S. institutional investor ''level of assets are more likely to have the skills and experience to assess independently the integrity and competence of the foreign broker-dealers providing [foreign market] access.''[48] As discussed below, we believe that advancements in communications and other technology have made it increasingly likely that a broader range of persons would have these skills and experience at a lower asset level.

The proposed rule would give the term ''qualified investor'' the same meaning as set forth in Section 3(a)(54) of the Exchange Act.[49] The qualified investor standard is well known to the financial community. Section 3(a)(54)(A) defines a ''qualified investor'' as:

(i) Any investment company registered with the Commission under Section 8 of the Investment Company Act of 1940 (''Investment Company Act'');

(ii) Any issuer eligible for an exclusion from the definition of investment company pursuant to Section 3(c)(7) of the Investment Company Act;

(iii) Any bank (as defined in Section 3(a)(6) of the Exchange Act), savings association (as defined in Section 3(b) of the Federal Deposit Insurance Act), broker, dealer, insurance company (as defined in Section 2(a)(13) of the Securities Act), or business development company (as defined in Section 2(a)(48) of the Investment Company Act);

(iv) Any small business investment company licensed by the United States Small Business Administration under Section 301(c) or (d) of the Small Business Investment Act of 1958;

(v) Any State sponsored employee benefit plan, or any other employee benefit plan, within the meaning of the Employee Retirement Income Security Act of 1974, other than an individual retirement account, if the investment decisions are made by a plan fiduciary, as defined in Section 3(21) of that Act, which is either a bank, savings and loan association, insurance company, or registered investment adviser;

(vi) Any trust whose purchases of securities are directed by a person described in clauses (i) through (v) above;

(vii) Any market intermediary exempt under Section 3(c)(2) of the Investment Company Act;

(viii) Any associated person of a broker or dealer other than a natural person;

(ix) Any foreign bank (as defined in Section 1(b)(7) of the International Banking Act of 1978);[50]

(x) The government of any foreign country;[51]

(xi) Any corporation, company, or partnership that owns and invests on a

[43] *See, e.g.,* Spotlight On: Roundtable Discussions Regarding Mutual Recognition (Jun. 12, 2007) (available at: *http://www.sec.gov/spotlight/mutualrecognition.htm).*

[44] *See, e.g., id.*

[45] *See* Part III.G., *infra*, regarding the scope of the exemption.

[46] The definition of ''foreign broker or dealer ''in the proposed rule would be the same as in the current rule, except as described below. *See* proposed Rule 15a–6(b)(2).

[47] The proposed rule would also eliminate the definition of ''family of investment companies,'' which is currently used in the definition of ''major U.S institutional investor, ''because it would no longer be needed. *See* 17 CFR 240.15a–6(b)(1), (4) and (7).

[48] 1989 Adopting Release, 54 FR at 30027. In proposing the definition of ''U.S. institutional investor,'' the Commission stated that ''[t]he proposed asset limitation in the rule is based on the assumption that direct U.S. oversight of the competence and conduct of foreign sales personnel may be of less significance where they are soliciting only U.S. institutional investors with high levels of assets. The $100 million asset level * * * is designed to increase the likelihood that the institution or its investment advisers have prior experience in foreign markets that provides insight into the reliability and reputation of various foreign broker-dealers.'' 1988 Proposing Release, 53 FR 23654.

[49] 15 U.S.C. 78c(54). The definition of ''qualified investor'' was added to the Exchange Act by the Gramm-Leach-Bliley-Act of 1999 (Pub. L. 106–102, 113 Stat. 1338 (1999)) and has application to several of the bank exceptions from broker-dealer registration, including: (1) the broker exception for identified banking products when the product is an equity swap agreement (Section 206(a)(6) of Pub. L. 106–102, 15 U.S.C. 78c note, as incorporated into Exchange Act Section 3(a)(4)(B)(ix), 15 U.S.C. 78c(a)(4)(B)(ix)); (2) the dealer exception for identified banking products when the product is an equity swap agreement (Section 206(a)(6) of Pub. L. 106–102, 15 U.S.C. 78c note, as incorporated into Exchange Act Section 3(a)(5)(C)(iv), 15 U.S.C. 78c(a)(5)(C)(iv)); and (3) the dealer exception for asset-backed securities (Exchange Act Section 3(a)(5)(C)(iii), 15 U.S.C. 78c(a)(5)(C)(iii)). These exceptions permit banks to sell certain securities to qualified investors without registering as broker-dealers with the Commission.

[50] The definition of qualified investor includes any foreign bank. Unlike foreign governments (*see* note 51, *infra*), foreign banks may establish a permanent presence in the United States, such as a branch, that would not qualify under Exchange Act Section 3(a)(6) as a bank. *See* note 1, *supra*. Foreign broker-dealers need to rely on Rule 15a–6 to effect transactions with such entities.

[51] Of course, foreign broker-dealers currently do not need to rely on Rule 15a–6 to effect transactions with foreign governments because foreign governments are neither located in the United States nor U.S. persons resident abroad.

discretionary basis not less than $25,000,000 in investments;

(xii) Any natural person who owns and invests on a discretionary basis not less than $25,000,000 in investments;

(xiii) Any government or political subdivision, agency, or instrumentality of a government that owns and invests on a discretionary basis not less than $50,000,000 in investments; or

(xiv) Any multinational or supranational entity or any agency or instrumentality thereof.

The Commission proposes to use the definition of ''qualified investor'' in section 3(a)(54) of the Exchange Act for several reasons primarily related to the sophistication and likely experience with foreign securities and foreign markets of the investors included in the definition. For example, the entities described in paragraphs (i) through (ix) of Section 3(a)(54)(A) of the Exchange Act, without limitation based on ownership or investment, are all engaged primarily in financial activities, including the business of investing. The persons in paragraphs (xi), (xii) and (xiii) of Section 3(a)(54)(A) are not primarily engaged in investing and may have limited investment experience. Thus, Congress established ownership and investment thresholds for those latter persons as indicators of investment experience and sophistication.[52] The Commission believes that Congress' standard for investors with significant investment experience and sophistication to deal with banks that are not registered as broker-dealers should ensure that these investors would possess sufficient experience with financial matters to be able to enter into securities transactions with foreign broker-dealers under the proposed exemption. Thus, the Commission believes that it would be appropriate and consistent with the protection of investors to extend the relief in proposed Rules 15a–6(a)(2) and (a)(3) to a corporation, company, partnership that, or a natural person who, owns and invests on a discretionary basis not less than $25,000,000 in investments, and to a government or political subdivision, agency or instrumentality of a government that owns and invests on a discretionary basis not less than $50,000,000 in investments.

The primary distinction between a major U.S. institutional investor and a qualified investor is the threshold value of assets or investments owned or invested and the inclusion of natural persons. As a result, under the proposed rule, the threshold would decline from institutional investors that own or control greater than $100 million in total assets to, among others, all investment companies registered with the Commission under Section 8 of the Investment Company Act and corporations, companies, or partnerships that own or invest on a discretionary basis $25 million or more in investments. In addition, under the proposed rule, natural persons who own or invest on a discretionary basis not less than $25,000,000 in investments would be included. In adopting Rule 15a–6, we explained that the $100 million asset level was designed ''to increase the likelihood that [the investor has] prior experience in foreign markets that provides insight into the reliability and reputation of various foreign broker-dealers.''[53] While we believe this is still the right focus, increased access to information about foreign securities markets due to advancements in communication technology suggest that a broader spectrum of investors are likely to have this type of sophistication.

We believe that the proposed use of the definition of qualified investor would more accurately encompass persons that have prior experience in foreign markets and an appropriate level of investment experience and sophistication overall. In certain instances, it would exclude persons that are currently included in the definition of U.S. institutional investor or major U.S. institutional investor. In each such instance, the proposed use of the definition of qualified investor would require greater investment experience of the entity than the current definition.

For example, with respect to employee benefit plans, the definition of qualified investor includes plans in which investment decisions are made by certain plan fiduciaries. The definition of U.S. institutional investor does not require a fiduciary to make investment decisions and encompasses plans with $5 million or more in assets. While there is no asset requirement in the employee benefit plan section in the definition of qualified investor, the Commission believes that proposing to require investment decisions to be made by plan fiduciaries as a qualification for the definition would help ensure a higher level of investing experience and sophistication than a $5 million asset threshold. Similarly, while a qualified investor applies to trusts whose purchases are directed by certain entities, the definition of ''U.S. institutional investor'' does not impose that limitation, but instead applies to certain trusts with $5 million or more in assets. Also, while the proposed definition (like the existing definition) would encompass business development companies as defined in Section 2(a)(48) of the Investment Company Act, the definition of ''U.S. institutional investor'' extends to private business development companies defined in Section 202(a)(22) of the Investment Advisers Act of 1940. The definition of ''U.S. institutional investor,'' unlike the definition of ''qualified investor,'' further applies to certain organizations described in Section 503(c) of the Internal Revenue Code with assets of $5 million or more. Proposing to require the higher level of investing experience and sophistication would be appropriate in light of the expanded activities in which foreign broker-dealers would be permitted to engage under the proposed rule, as well as the reduced role that would be played by the U.S. registered broker-dealer.

The Commission requests comment on the proposed use of the definition of ''qualified investor'' generally and, more specifically, whether allowing foreign broker-dealers to induce or attempt to induce transactions with the persons included in the proposed definition is appropriate. Are the ownership and investment thresholds applicable to certain persons included in the proposed use of the definition of ''qualified investor'' appropriate? Does the definition encompass investors that likely would have an appropriate level of investing or business experience in foreign markets? If not, why not? Should the definition be tailored to include only investors that have a demonstrated pattern of appropriate transactional activity with U.S. registered or foreign broker-dealers in foreign securities? If so, how?

The Commission also requests comment on whether the proposed use of the definition of ''qualified investor'' should include additional minimum asset levels for any of the persons included in Exchange Act Section 3(a)(54). For example, should the proposed rule use a new definition that includes a requirement that a small business investment company own and invest a certain amount of investments? Should it include any of the omitted

[52] *See* 15 U.S.C. 6801 *et seq.,* Pub. L. 106–102, 113 Stat. 1338 (1999). Congress did not include an ownership or investment threshold for multinational or supranational entities, or any agencies or instrumentalities thereof, presumably regarding such entities as possessing sufficient financial sophistication, net worth and knowledge and experience in financial matters to be considered a qualified investor. Exchange Act Release No. 47364 (Feb. 13, 2003), 68 FR 8686, 8693 (Feb. 24, 2003).

[53] *See* 1989 Adopting Release, 54 FR at 30027.

categories of persons from the definition of ''U.S. institutional investor''? Are there any categories of investors included in the proposed use of the definition of qualified investor that should be excluded, such as market intermediaries exempt under Section 3(c)(2) of the Investment Company Act?

In addition, the Commission requests comment on whether the proposed use of the definition of ''qualified investor'' should include natural persons who own or invest on a discretionary basis at least $25,000,000 in investments. If not, should the Commission adopt a different threshold level of investments or ownership? What criteria, if any, should apply to help ensure that a natural person would have sufficient investment experience and sophistication specifically in foreign securities? Are there additional safeguards for natural persons that would be appropriate to include in the rule, such as increasing the involvement of U.S. registered broker-dealers in transactions solicited by foreign broker-dealers? For example, foreign broker-dealers could be required to make suitability determinations before sales to natural persons under the exemption. If additional safeguards applied to transactions with natural persons who own or invest on a discretionary basis at least $25,000,000 in investments, would foreign broker-dealers choose to comply with those safeguards or choose not to do business directly with natural persons under such a rule? Finally, should any of the dollar thresholds in the proposed use of the definition of qualified investor be adjusted for inflation? If so, what mechanism should be used to make such adjustments?

B. Unsolicited Trades

As we noted in adopting Rule 15a–6, although the requirements of Section 15(a) under the Exchange Act do not distinguish between solicited and unsolicited transactions, the Commission does not believe, as a policy matter, that registration is necessary if U.S. investors have sought out foreign broker-dealers outside the United States and initiated transactions in foreign securities markets entirely of their own accord.[54] In that event, U.S. investors would have taken the initiative to trade outside the United States with foreign broker-dealers that are not conducting activities within this country and the U.S. investors would have little reason to expect these foreign broker-dealers to be subject to U.S. broker-dealer requirements.[55] Therefore, the Commission is not proposing to amend paragraph (a)(1) of the current rule, other than to add the title ''Unsolicited Trades.'' Notably, in order to rely on this exemption, foreign broker-dealers need to determine whether each transaction effected in reliance on it has been solicited under the proposed rule.

Because the Commission construes solicitation broadly and relatively few transactions qualify for the unsolicited exemption,[56] the Commission is proposing to provide further interpretive guidance related to solicitation under the proposed rule with respect to quotation systems. In adopting the current rule, we noted that access to foreign market makers' quotations is of considerable interest to registered broker-dealers and institutional investors that seek timely information on foreign market conditions.[57] The Commission also stated that it generally would not consider a solicitation to have occurred for purposes of Rule 15a–6 if there were a U.S. distribution of foreign broker-dealers' quotations by third-party systems, such as systems operated by foreign marketplaces or by private vendors, that distributed these quotations primarily in foreign countries.[58] The Commission's position applies only to third-party systems that do not allow securities transactions to be executed between the foreign broker-dealer and persons in the United States through the systems.[59] The Commission noted that it would have reservations about certain specialized quotation systems, which might constitute a more powerful inducement to effect trades because of the nature of the proposed transactions.[60] With respect to direct dissemination of a foreign market maker's quotations to U.S. investors, such as through a private quote system controlled by a foreign broker-dealer (as distinct from a third-party system), the Commission noted in adopting the current rule that such conduct would not be appropriate without registration, because the dissemination of these quotations would be a direct, exclusive inducement to trade with that foreign broker-dealer.[61]

Since the time the current rule was adopted, third-party quotation systems have become increasingly global in scope such that the distinction between systems that distribute quotations primarily in the United States and those that distribute quotations primarily in foreign countries is no longer a meaningful or workable distinction because most third-party quotation systems no longer serve a primary location.[62] As a result, under the Commission's proposed interpretation, the Commission's previous guidance on U.S. distribution of foreign broker-dealers' quotations by third-party systems no longer would be limited to third-party systems that distributed their quotations primarily in foreign countries under the proposed rule. In other words, under the proposed interpretation, U.S. distribution of foreign broker-dealers' quotations by a third-party system (which did not allow securities transaction to be executed between the foreign broker-dealer and persons in the U.S. through the system) would not be viewed as a form of solicitation, in the absence of other contacts with U.S. investors initiated by the third-party system or the foreign broker-dealer.

The Commission seeks comment regarding whether retaining the proposed Unsolicited Trades exemption in paragraph (a)(1) is appropriate. Are any modifications to this exemption necessary to reflect increasing internationalization in securities markets and advancements in technology and communication services since the exemption was adopted in 1989? Commenters are invited to provide information on the specific circumstances in which foreign broker-dealers use the exemption in paragraph (a)(1) of the current rule and particularly on the frequency of its use. The Commission also seeks comment on its proposed interpretation with respect to third-party quotation systems under the proposed rule. Are there other interpretive issues relating to third-party

[54] *See* 1989 Adopting Release, 54 FR at 30017.

[55] *See id.*

[56] *See id.* at 30021.

[57] *See id.* at 30017.

[58] *See id.*

[59] *See id.*

[60] *See id.* at n.66. For example, the Commission stated that a foreign broker-dealer whose quotations were displayed in a system that disseminated quotes only for large block trades might well be deemed to have engaged in solicitation requiring broker-dealer registration, as opposed to a foreign broker-dealer whose quotes were displayed in a system that disseminated the quotes of numerous foreign dealers or market makers in the same security. *See id.*

[61] *See id.* at 30019. In making the statement that the conduct would not be appropriate ''without registration, ''the Commission did not intend to preclude a foreign broker-dealer from directly inducing U.S. investors to trade with the foreign broker-dealer via such a quotation system where the U.S. investor subscribes to the quotation system through a U.S. broker-dealer, the U.S. broker-dealer has continuing access to the quotation system, the foreign broker-dealer's other contacts with the U.S. investor are permissible under the current rule and any resulting transactions are intermediated in accordance with the requirements of Rule 15a–6(a)(3).

[62] *Cf.* 1997 Staff Letter.

quotation systems, or proprietary quotation systems, that the Commission should address? Is guidance needed under the Commission's interpretation of solicitation for other entities, such as third-party or proprietary systems that provide indications of interest, for purposes of the proposed amendments of Rule 15a–6?

Because one of the requirements for being an alternative trading system under Regulation ATS[63] is to be registered as a broker-dealer under Section 15(b) of the Exchange Act, a foreign broker-dealer relying on an exemption in proposed Rule 15a–6 would not be eligible to rely on the exemption in Regulation ATS. The Commission solicits comment on whether it should consider amending Regulation ATS to allow a foreign broker-dealer relying on an exemption in proposed Rule 15a–6 to operate an alternative trading system in the United States so long as it otherwise complies with the terms of Regulation ATS.

C. Provision of Research Reports

The provision of research to investors also may constitute solicitation by a broker-dealer, in part because broker-dealers often provide research to customers on a non-fee basis, with the expectation that the customers eventually will trade through the broker-dealer.[64] As we noted in adopting Rule 15a–6, the Commission does not wish to restrict the ability of U.S. investors to obtain foreign research reports in the United States if adequate regulatory safeguards are present.[65] Therefore, the Commission would retain the current exemption for the provision of research reports in paragraph (a)(2) of the current rule. However, for the reasons discussed above,[66] the Commission is proposing to expand the class of investors to which the foreign broker-dealer could provide research reports directly from major U.S. institutional investors to qualified investors. As proposed, paragraph (a)(2) would permit a foreign broker-dealer, subject to the conditions discussed below, to furnish research reports to qualified investors and effect transactions in the securities discussed in the research reports with or for those qualified investors.

Paragraph (a)(2) of the proposed rule would retain the conditions in current Rule 15a–6(a)(2), modified solely to reflect the proposed expansion of the class of investors to qualified investors. Specifically, proposed paragraph (a)(2) would be available, provided that: (1) The research reports do not recommend the use of the foreign broker-dealer to effect trades in any security; (2) the foreign broker-dealer does not initiate contact with the qualified investors to follow up on the research reports and does not otherwise induce or attempt to induce the purchase or sale of any security by the qualified investors; (3) if the foreign broker-dealer has a relationship with a registered broker-dealer that satisfies the requirements of paragraph (a)(3) of the proposed rule, any transactions with the foreign broker-dealer in securities discussed in the research reports are effected pursuant to the provisions of paragraph (a)(3); and (4) the foreign broker-dealer does not provide research to U.S. persons pursuant to any express or implied understanding that those U.S. persons will direct commission income to the foreign broker-dealer. We understand from discussions with industry representatives that these conditions have been workable for both foreign broker-dealers and U.S. registered broker-dealers and we have no knowledge of investor protection concerns having been raised with regard to foreign broker-dealers that operate in compliance with the current exemption. Accordingly, we do not propose to amend them.

If these conditions are met, the Commission proposes to allow the foreign broker-dealer to effect transactions in the securities discussed in a research report at the request of a qualified investor. The Commission believes that, under the proposed conditions, the direct distribution of research to qualified investors would be consistent with the free flow of information across national boundaries without raising substantial investor protection concerns.[67]

The Commission seeks comment on the proposed ''Research Reports'' exemption in paragraph (a)(2). Should any of the conditions of the current exemption be changed to address the proposed expansion of the class of institutional investors to which research reports may be distributed directly, or to reflect increasing internationalization in securities markets and advancements in technology and communication services since the exemption was adopted in 1989? If so, how? Similarly, should any of the conditions of the current exemption be changed to more closely align with the proposed modifications to the requirements of paragraph (a)(3) discussed below in Part III.D.? If so, how? Commenters are invited to provide information on the specific circumstances in which foreign broker-dealers use the exemption in paragraph (a)(2) of the current rule and on the frequency of its use.

D. Solicited Trades

The proposed rule would significantly revise the conditions under which a foreign broker-dealer could induce or attempt to induce the purchase or sale of a security by certain U.S. investors under paragraph (a)(3) of Rule 15a–6. Overall, and as discussed more fully below, the proposed rule would reduce and streamline the obligations of the U.S. registered broker-dealer in connection with these transactions and, in certain situations, permit a foreign broker-dealer to provide full-service brokerage by effecting securities transactions on behalf of qualified investors and maintaining custody of qualified investor funds and securities relating to any resulting transactions.

1. Customer Relationship

The proposed rule would require a foreign broker-dealer that induces or attempts to induce the purchase or sale of any security by a qualified investor to engage a U.S. registered broker-dealer under one of two exemptive approaches, to which we will refer as Exemption (A)(*1*) and Exemption (A)(*2*), corresponding to paragraphs (a)(3)(iii)(A)(*1*) and (A)(*2*) of the proposed rule.[68] As explained below, under both proposed exemptions, the U.S. registered broker-dealer would have fewer obligations than under paragraph (a)(3) of the current rule and the foreign broker-dealer would correspondingly be permitted to play a greater role in effecting any resulting transactions. Both proposed exemptions would allow qualified investors the more direct contact they seek with those expert in foreign markets and foreign securities, without certain barriers such as the chaperoning requirements that may be unnecessary in light of other protections and investor sophistication. Nevertheless, as explained below, both proposed exemptions would retain important measures of investor protection that the Commission believes would, among other things, address the potential risks to qualified investors related to contacts with foreign associated persons with a disciplinary history and ensure that the books and records related to transactions for U.S. investors are available to the Commission.

[63] *See* 17 CFR 242.300 *et seq.*

[64] *See* 1989 Adopting Release, 54 FR at 30021.

[65] *See id.*

[66] *See* Part III.A., *supra*.

[67] *See* 1989 Adopting Release, 54 FR at 30021.

[68] *See* proposed Rule 15a–6(a)(3)(iii)(A).

There are two primary differences between the two proposed exemptive approaches. First, Exemption (A)(*1*) could only be used by foreign broker-dealers that conduct a ''foreign business,'' [69] while Exemption (A)(*2*) could be used by all foreign broker-dealers. Second, the foreign broker-dealer would be permitted to custody funds and securities of qualified investors in connection with resulting transactions under Exemption (A)(*1*), but not under Exemption (A)(*2*). These distinctions are discussed in the following paragraphs.

a. Exemption (A)(*1*)

i. Role of the U.S. Registered Broker-Dealer

For transactions effected by a foreign broker-dealer pursuant to proposed Exemption (A)(*1*),[70] a U.S. registered broker-dealer would be required to maintain copies of all books and records, including confirmations and statements issued by the foreign broker-dealer to the qualified investor, relating to any such transactions.[71] As discussed below, the proposed rule would allow such books and records to be maintained by the U.S. registered broker-dealer in the form, manner and for the periods prescribed by the foreign securities authority (as defined in Section 3(a)(50) of the Exchange Act) [72] regulating the foreign broker-dealer.[73] The proposed rule would give the term ''foreign securities authority'' the same meaning as set forth in Section 3(a)(50) of the Exchange Act,[74] which defines ''foreign securities authority'' to mean ''any foreign government, or any governmental body or regulatory organization empowered by a foreign government to administer or enforce its laws as they relate to securities matters.''

Because proposed Exemption (A)(*1*) would allow a foreign broker-dealer to effect transactions for qualified investors and custody their funds and assets, the foreign broker-dealer would generate books and records relating to the transactions. Proposed Exemption (A)(*1*) would allow the U.S. registered broker-dealer to maintain such books and records with the foreign broker-dealer, provided that the U.S. registered broker-dealer makes a reasonable determination that copies of any or all of such books and records could be furnished promptly to the Commission and promptly provides any such books and records to the Commission, upon request.[75] In making such a determination, the U.S. registered broker-dealer would need to consider, among other things, the existence of any legal limitations in the foreign jurisdiction that might limit the ability of the foreign broker-dealer to disclose information relating to transactions conducted pursuant to proposed Exemption (A)(*1*) to the U.S. registered broker-dealer. Proposing to require U.S. registered broker-dealers to make a reasonable determination that the books and records could be furnished promptly to the Commission is designed to ensure that the ability of the Commission to obtain copies of the books and records would not be diminished. It should also significantly reduce the U.S. registered broker-dealer's cost of recordkeeping with respect to transactions effected pursuant to this exemption. Thus, the Commission believes that allowing U.S. registered broker-dealers to maintain books and records with a foreign broker-dealer would appropriately support the Commission's interest in the protection of investors—by being designed to ensure that the books and records related to transactions for U.S. investors are available to the Commission—while avoiding the burden that might be placed on U.S. registered broker-dealers under the exemption by requiring the books and records to be maintained in the form, manner and for the periods prescribed by Rules 17a–3 and 17a–4 under the Exchange Act,[76] as if the U.S. registered broker-dealer had effected the transactions under proposed Exemption (A)(*1*).

Unlike under the current rule, under Exemption (A)(*1*), the intermediating U.S. registered broker-dealer would not be required to effect all aspects of the transaction.[77] Thus, with respect to transactions effected pursuant to Exemption (A)(*1*), the intermediating U.S. registered broker-dealer would no longer be required to comply with the provisions of the federal securities laws, the rules thereunder and SRO rules applicable to a broker-dealer effecting a transaction in securities, unless it were otherwise involved in effecting the transaction.[78] However, if a foreign broker-dealer effects a transaction pursuant to Exemption (A)(*1*) on a U.S. national securities exchange, through a U.S. alternative trading system, or with a market maker or an over-the-counter dealer in the United States, as is common with respect to U.S. securities, a U.S. registered broker-dealer would be involved in effecting the transaction and would be required to comply with the provisions of the federal securities laws, the rules thereunder and SRO rules applicable to such activity. In other words, such provisions would apply with respect to all transactions in U.S. securities under Exemption (A)(*1*) other than certain over-the-counter transactions that a foreign broker-dealer does not effect by or through a U.S. registered broker-dealer.

The intermediating U.S. registered broker-dealer also would no longer be required to extend or arrange for the extension of credit, issue confirmations and account statements, comply with Rule 15c3–1 with respect to the transactions, or receive, deliver and safeguard funds and securities in connection with the transactions in compliance with Rule 15c3–3.[79] In addition, the intermediating U.S. registered broker-dealer would no longer be required to maintain accounts for the customers of foreign broker-dealers relying on Exemption (A)(*1*),[80] or comply with the requirements applicable to broker-dealers that maintain such accounts. As a result, among other requirements, the U.S. registered broker-dealer may not have obligations under Exchange Act Rule 17a–8 [81] with respect to customers of foreign broker-dealers relying on Exemption (A)(*1*). Rule 17a–8 requires a

[69] *See* Part III.D.1.a.ii., *infra*, for discussion of ''foreign business.''

[70] As mentioned above and discussed more fully below, only foreign broker-dealers that conduct a ''foreign business ''would be eligible to effect transactions on behalf of qualified investors pursuant to Exemption (A)(*1*).

[71] *See* proposed Rule 15a–6(a)(3)(iii)(A)(*1*). Of course, this would not prevent the U.S. registered broker-dealer from performing other aspects of the transaction.

[72] 15 U.S.C. 78c(a)(50).

[73] *See* proposed Rule 15a–6(a)(3)(iii)(A)(*1*). Of course, this would not change any books and recordkeeping obligations a U.S. registered broker-dealer may have under Exchange Act Rules 17a–3 and 17a–4 (17 CFR 240.17a–3 and 17a–4).

[74] 15 U.S.C. 78c(a)(50).

[75] *See* Exchange Act Release No. 44992 (Oct. 26, 2001), 66 FR 55818, 55825 & n.72 (Nov. 2, 2001) (''Generally, requests for records which are readily available at the office (either on-site or electronically) should be filled on the day the request is made. If a request is unusually large or complex, then the firm should discuss with the regulator a mutually agreeable time-frame for production. * * * Valid reasons for delays in producing the requested records do not include the need to send the records to the firm's compliance office for review prior to providing the records.'').

[76] *See* 17 CFR 240.17a–3 and 17a–4.

[77] *See* 17 CFR 240.15a–6(a)(3)(iii)(A) (requiring the U.S. registered broker-dealer to effect all aspects of a transaction other than negotiation of its terms) and proposed Rule 15a–6(a)(3)(iii)(A)(*1*); *see also* note 28, *supra*, for a discussion of the differing treatment of U.S. and foreign securities under current Rule 15a–6(a)(3)(iii)(A)(*1*).

[78] *See* note 28, *supra*, for a discussion of the differing treatment of U.S. and foreign securities under current Rule 15a–6(a)(3)(iii)(A)(*1*).

[79] *See* 17 CFR 240.15a–6(a)(3)(iii)(A)(*1*), (*2*), (*3*), (*4*) and (*5*) and the discussion in Part II.C., *supra*.

[80] *See* text accompanying note 38, *supra*.

[81] 17 CFR 240.17a–8.

U.S. registered broker-dealer to comply with the reporting, recordkeeping and record retention requirements in regulations implemented under the Bank Secrecy Act.[82] As discussed above, current Rule 15a–6 permits an unregistered foreign broker-dealer to effect transactions directly with U.S. persons on an unsolicited basis,[83] and to solicit certain U.S. institutional investors by means of research reports and effect transactions in securities discussed in such reports, subject to certain conditions,[84] in either case without intermediation by a U.S. registered broker-dealer subject to Rule 17a–8. Would permitting a foreign broker-dealer to effect securities transactions on a solicited basis with certain U.S. persons under proposed Exemption (A)(*1*) present any concerns with respect to Rule 17a–8 or anti-money laundering obligations under the Bank Secrecy Act? How should these concerns, if any, be addressed? For example, are there specific circumstances in which the Commission should consider imposing additional obligations on the U.S. registered broker-dealer or the foreign broker-dealer under proposed Exemption (A)(*1*) or alternatively prohibiting the use of Exemption (A)(*1*)?

The Commission requests comment generally on the proposed requirements in Exemption (A)(*1*) of the proposed rule. In particular, the Commission requests comment on whether the Commission should require the U.S. registered broker-dealer to comply with any requirements with respect to transactions under Exemption (A)(*1*) other than the proposed requirement to maintain books and records relating to the transactions. Should the requirements differ based on whether the securities are U.S. securities or foreign securities? If so, why and how? The Commission also requests comment on whether the Commission should require the U.S. registered broker-dealer to maintain books and records relating to the transactions in the form, manner and for the periods prescribed by Rules 17a–3 and 17a–4 under the Exchange Act as if the U.S. registered broker-dealer had effected the transactions under Exemption (A)(*1*). In addition, the Commission requests comment on whether the Commission should permit the U.S. registered broker-dealers to maintain copies of books and records resulting from transactions under paragraph Exemption (A)(*1*) with the foreign broker-dealer. Should it depend on the adequacy of the books and recordkeeping requirements to which the foreign broker-dealer is subject? Should the Commission provide more guidance on or should the proposed rule provide parameters for what would constitute a reasonable determination? In lieu of the proposed requirement of a reasonable determination by the U.S. registered broker-dealer under Exemption (A)(*1*), should the Commission condition the exemption on the foreign broker-dealer filing a written undertaking with the Commission to furnish the books and records to the U.S. registered broker-dealer or the Commission upon request?

Furthermore, the Commission requests comment on whether the requirement under Exemption (A)(*1*) that the U.S. registered broker-dealer make a reasonable determination that books and records relating to any resulting transactions could be furnished promptly to the Commission upon request, and promptly provide such books and records to the Commission upon request, is the appropriate standard given the potential time-zone differences and the fact that such records may be maintained in paper form. If not, what is the appropriate standard and why?

ii. Role of the Foreign Broker-Dealer

The proposed rule would limit the availability of Exemption (A)(*1*) to foreign broker-dealers that are regulated for conducting securities activities (such as effecting transactions in securities), including the specific activities in which the foreign broker-dealer engages with the qualified investor, in a foreign country by a foreign securities authority.[85] This requirement is designed to ensure that only foreign entities that are legitimately in the business of conducting securities activities (such as effecting transactions in securities), and that are regulated in the conduct of those activities, could rely on Exemption (A)(*1*).

Both Exemption (A)(*1*) and Exemption (A)(*2*) would require the foreign broker-dealer to disclose to the qualified investor that it is regulated by a foreign securities authority and not by the Commission. Unlike under Exemption (A)(*2*), for the reasons discussed below,[86] the foreign broker-dealer operating under proposed Exemption (A)(1) would also be required to disclose that U.S. segregation requirements (*e.g.*, the requirement that customer funds and assets be segregated from the broker-dealer's own proprietary funds and assets), U.S. bankruptcy protections (*e.g.*, preference to creditors in bankruptcy) and protections under the Securities Investor Protection Act (''SIPA'')[87] will not apply to any funds and securities of the qualified investor held by the foreign broker-dealer.[88]

These disclosure requirements are intended to help to put qualified investors on notice that foreign broker-dealers operating pursuant to Exemption (A)*(1)* of the proposed rule would not be subject to the same regulatory requirements as U.S. registered broker-dealers. This notice would be important because the proposed rule would eliminate the current chaperoning requirements, as described below, and allow a foreign broker-dealer to effect transactions on behalf of qualified investors and custody qualified investor funds and securities relating to any resulting transactions with more limited participation in the transactions by a U.S. registered broker-dealer. This should be sufficient notice given the level of sophistication of the investors with which the foreign broker-dealer would be engaging in transactions under Exemption (A)*(1)*. Specifically, proposing to require disclosure that the foreign broker-dealer is regulated by a foreign securities authority and not the Commission should alert qualified investors that the foreign broker-dealer would not be subject to the full scope of the Commission's broker-dealer regulatory framework. Proposing to require disclosure that U.S. segregation requirements, U.S. bankruptcy protection and protections under the SIPA would not apply to the funds and securities of the qualified investor held by the foreign broker-dealer should alert the qualified investor that its funds and assets would not receive the same protections that they would under U.S. law.

Exemption (A)*(1)* would only be available to foreign broker-dealers that

[82] Currency and Foreign Transactions Reporting Act of 1970 (commonly referred to as the Bank Secrecy Act). *See* 31 U.S.C. 5311 et seq., 12 U.S.C. 1829b and 12 U.S.C. 1951–1959. The Secretary of the U.S. Department of Treasury has delegated responsibility for the administration of the Bank Secrecy Act to the Director of the Financial Crimes Enforcement Network (''FinCEN''), a bureau of the U.S. Department of Treasury. *See* Treasury Order 180–01 (Sep. 26, 2002).

[83] *See* Part II.A., *supra*.

[84] *See* Part II.B., *supra*.

[85] *See* proposed Rule 15a–6(b)(2)(i).

[86] *See* Part III.D.b.ii., *infra*.

[87] 15 U.S.C. 78aaa *et seq*. The SIPA created the Securities Investor Protection Corporation (''SIPC''), a nonprofit, private membership corporation to which most registered brokers and dealers are required to belong, and established a fund administered by SIPC designed to protect the customers of brokers or dealers subject to the Act from loss in case of financial failure of the member.

[88] *See* proposed Rule 15a–6(a)(3)(i)(D)(1) and (2).

conduct a ''foreign business.''[89] As explained below, the proposed rule would define ''foreign business'' to mean the business of a foreign broker-dealer with qualified investors and foreign resident clients[90] where at least 85% of the aggregate value of the securities purchased or sold in transactions conducted pursuant to both paragraphs (a)(3) and (a)(4)(vi) of the proposed rule by the foreign broker-dealer, calculated on a rolling two-year basis, is derived from transactions in foreign securities, as defined below.[91] In general, the Commission believes that making Exemption (A)*(1)* available only to a foreign broker-dealer conducting a foreign business would provide U.S. investors increased access to foreign securities and markets without creating opportunities for regulatory arbitrage vis-á-vis U.S. securities markets because the foreign broker-dealer's business in U.S. securities would be limited.

The proposed definition of foreign securities would include both debt and equity securities of foreign private issuers and debt securities of issuers organized or incorporated in the United States but where the distribution is wholly outside the United States in compliance with Regulation S, as well as certain securities issued by foreign governments. The proposed definition is not restricted to certain types of securities, rather, to the extent that qualified investors are interested in purchasing foreign securities, the Commission believes that they should be able to access a broad range of foreign securities. The proposed rule would define ''foreign securities'' to mean:

(i) An equity security (as defined in 17 CFR 230.405) of a foreign private issuer (as defined in 17 CFR 230.405);[92]

(ii) A debt security (as defined in 17 CFR 230.902) of a foreign private issuer (as defined in 17 CFR 230.405);

(iii) A debt security (as defined in 17 CFR 230.902) issued by an issuer organized or incorporated in the United States in connection with a distribution conducted solely outside the United States pursuant to Regulation S (17 CFR 230.903 *et seq.*);[93]

(iv) A security that is a note, bond, debenture or evidence of indebtedness issued or guaranteed by a foreign government (as defined in 17 CFR 230.405) that is eligible to be registered with the Commission under Schedule B of the Securities Act; and

(v) A derivative instrument on a security described in subparagraph (i), (ii), (iii), or (iv) of this paragraph.[94]

The proposed rule would require the foreign broker-dealer to compute the absolute value of all transactions pursuant to both paragraphs (a)(3) and (a)(4)(vi) of the proposed rule (*i.e.*, without netting the transactions) each year to determine the aggregate amount for the previous two years. For example, a foreign broker-dealer that sold 100 shares of Security A at $10.00 per share and bought 100 shares of Security A at $10.00 per share pursuant to paragraphs (a)(3) and (a)(4)(vi) of the proposed rule would have an aggregate value of securities bought and sold of $2000.00 (or (100 × $10.00) + (100 × $10.00)).

We note that the definition of foreign security would include, among other things, derivative instruments on debt and equity securities of foreign private issuers. Given that the proposed rule would provide an exemption for foreign broker-dealers that effect transactions in securities, the proposed definition of ''foreign securities'' would not include derivative instruments that are not themselves securities. Thus, foreign broker-dealers would not need to include the value of swap agreements that meet the definition of ''swap agreement'' in Section 206A of the Gramm-Leach-Bliley Act (''GLBA'') in the foreign business test calculation because they are excluded from the definition of security.[95] In the case of other derivative instruments that are securities, the valuation would depend on the product. For example, the value of options on a security or group or index of securities bought or sold would be the premium paid by the buyer, not the value of the underlying security or securities. Similarly, the value of a security future would be the price times the number of securities to be delivered at the time the transaction is entered into.

Foreign broker-dealers should be able to use this valuation information to calculate the total, combined value of the securities purchased or sold in transactions conducted pursuant to both paragraphs (a)(3) and (a)(4)(vi) of the proposed rule to determine the percentage of foreign securities bought from, or sold to, U.S. investors.

The calculation of the composition of the foreign broker-dealer's business on a rolling, two-year basis would mean that, after the first year the foreign broker-dealer relies on the exemption, the foreign broker-dealer would calculate the aggregate value of securities purchased and sold for the prior two years to determine whether it has complied with the foreign business test to be eligible for proposed Exemption (A)(*1*). This proposed requirement would allow for short-term fluctuations that otherwise could cause a foreign broker-dealer to be out of compliance with the exemption on isolated occasions. A foreign broker-dealer would have the flexibility to elect to use a calendar year or the firm's fiscal year for purposes of complying with the foreign business test. In addition, to provide foreign broker-dealers sufficient time to obtain and verify the relevant aggregate value data, the proposed rule would allow foreign broker-dealers to rely on the calculation made for the prior year for the first 60 days of a new year.[96] Hence, a foreign broker-dealer that had a foreign business over years 1 and 2 would be deemed to have a foreign business for the first 60 days of year 4, regardless of the result of the calculation for year 3. We believe that 60 days would be an appropriate ''grace period'' because it would give a foreign broker-dealer time to make the necessary calculation and to cease relying on Exemption (A)(*1*) if the calculation revealed that it was no longer conducting a foreign business.

Making Exemption (A)(*1*) available only to a foreign broker-dealer

[89] *See* proposed Rule 15a–6(b)(2)(ii).

[90] *See* Part III.E., *infra*.

[91] *See* proposed Rule 15a–6(b)(3).

[92] 17 CFR 230.405 defines ''foreign private issuer'' to mean any foreign issuer other than a foreign government, except issuers that meet the following conditions: (1) More than 50 percent of the outstanding voting securities of such issuer directly or indirectly owned of record by residents of the United States; and (2) any of the following: (i) the majority of the executive officers or directors are U.S. citizens or residents; (ii) more than 50 percent of the assets of the issuer are located in the United States; or (iii) the business of the issuer is administered principally in the United States. The rule sets forth guidelines for determining the percentage of outstanding voting securities owned of record by residents of the United States.

[93] Thus, debt securities of an issuer organized or incorporated under the laws of the United States would not qualify as ''foreign securities'' if they were offered and sold as part of a global offering involving both an offer and sale of the securities in the United States and a contemporaneous distribution outside the United States. This would be consistent with the purpose of the foreign business test, as discussed below.

[94] *See* proposed Rule 15a–6(b)(5).

[95] The GLBA defines ''swap agreement,'' in part, as an agreement between eligible contract participants (as defined in Section 1a(12) of the Commodity Exchange Act), the material terms of which (other than price and quantity) are subject to individual negotiation. Swap agreements may be based on a wide range of financial and economic interests. Section 206B of the GLBA defines ''security-based swap agreement'' as a swap agreement of which ''a material term is based on the price, yield, value, or volatility of any security or any group or index of securities, or any interest therein.'' Section 3A of the Exchange Act excludes from the definition of security both security-based swap agreements and ''non-security-based swap agreements.'' The Commission retains, however, antifraud authority (including authority over insider trading) over security-based swap agreements. *See, e.g.,* Section 10(b) of the Exchange Act.

[96] *See* proposed Rule 15a–6(b)(3).

conducting a foreign business would provide U.S. investors increased access to foreign securities and foreign markets without creating opportunities for regulatory arbitrage vis-á-vis U.S. securities markets because the foreign broker-dealer's business in U.S. securities would be limited. We believe this is particularly important because, under Exemption (A)(*1*), for the first time, a foreign broker-dealer would be able to provide full-service brokerage services (including maintaining custody of funds and securities from resulting transactions) to certain U.S. investors.

We are proposing an 85% percent threshold for determining whether a foreign broker-dealer conducts a foreign business because we understand from industry representatives that foreign broker-dealers currently effect transactions pursuant to paragraph (a)(3) of Rule 15a–6 primarily in foreign securities and only do a small percentage of business in U.S. securities (less than 10%, by most estimates). The Commission has not been given any indication that foreign broker-dealers would seek to use an expanded exemption to increase their business in U.S. securities. The 85% threshold should accommodate existing business models and allow foreign broker-dealers to continue to do a limited amount of business in U.S. securities, whether as an accommodation to their clients or as part of program trading (*i.e.*, any trading strategy involving the related purchase or sale of a group of stocks as part of a coordinated trading strategy, which could include U.S. securities), without causing those foreign broker-dealers to lose the benefit of the exemption. Any lower threshold could allow a foreign broker-dealer to conduct significant business in U.S. securities with certain U.S. investors without being subject to the full scope of the Commission's broker-dealer regulatory framework. This, in turn, could hinder the ability of the Commission to protect investors, maintain fair, orderly and efficient markets and facilitate capital formation,[97] as well as affect the competitive positions of U.S. registered broker-dealers and foreign broker-dealers.[98]

The Commission seeks comment on proposed Exemption (A)(*1*) generally. We invite comment on the proposed limitation of foreign broker-dealers to those that are regulated for conducting securities activities by a foreign securities authority and that conduct a foreign business. The Commission also seeks comment on whether the proposed disclosures provide appropriate notice to qualified investors that foreign broker-dealers would not be subject to the same regulatory requirements as U.S. registered broker-dealers. Would notice be sufficient? Are there other disclosures that should be required, in particular if the foreign jurisdiction does not require the segregation of qualified investor funds and assets or provide for bankruptcy protection for those funds and assets? Should the foreign broker-dealer be required to identify the foreign securities authority or authorities regulating the foreign broker-dealer? Should disclosure of the applicable dispute resolution system be required? In addition, the Commission requests comment regarding the proposed required form of these disclosures. Should the proposed disclosures be eliminated or modified in any way? If so, how and why?

The Commission solicits comment on the proposed definition of foreign broker-dealer. Should the proposed rule require a foreign broker-dealer to be regulated for conducting securities activities, including the specific activities in which the foreign broker or dealer engages with the qualified investor, in a foreign country by a foreign securities authority? What if foreign securities authorities do not apply their regulations to the activities of their broker-dealers outside their country or with non-residents? The Commission also seeks comment on the proposed definition of foreign securities.[99] Are there any other types of securities that should be included within the definition? Should any types of securities be excluded? Will reference to the equity and debt securities of a ''foreign private issuer,'' as that term is defined in 17 CFR 230.405, affect the interest of foreign issuers to cross-list on both foreign and U.S. exchanges? If so, how? Furthermore, will reference to the equity and debt securities of a ''foreign private issuer,'' as that term is defined in 17 CFR 230.405, affect listings of American Depositary Receipts issued by depositaries against the deposit of the securities of foreign issuers on U.S. exchanges? If so, how?

The Commission seeks comment on the proposed definition of ''foreign business.'' [100] Would the proposed test be workable? Would it be relatively easy for foreign broker-dealers to make the foreign business test calculation? Should the proposed test apply separately to debt and equity securities? Should the proposed test exclude U.S. government securities from the percentage of business in U.S. securities for purposes of computing the threshold? Is the proposed method of valuing options and security futures appropriate? Should we provide examples of how to value other types of derivative instruments?

The Commission requests comment on whether the proposed 85% threshold would be sufficient to enable foreign broker-dealers to effect transactions in U.S. securities as an accommodation and engage in program trading with qualified investors. Would compliance with the threshold be easily determinable? Should it be raised or lowered to better protect against regulatory arbitrage or to achieve its stated purposes? Commenters suggesting a different threshold or a different method for determining compliance with the threshold should explain why the Commission should choose that threshold or method. Instead of requiring foreign broker-dealers to conduct a ''foreign business,'' should Exemption (A)(*1*) of the proposed rule instead permit foreign broker-dealers to effect transactions in foreign securities and U.S. government securities, with a limited exemption for the purchase of U.S. securities by qualified persons as part of a program trade, provided that the purchase or sale of foreign securities predominates?

b. Exemption (A)(*2*)

Proposed Exemption (A)(*2*) is designed to be used by foreign broker-dealers that would like to solicit transactions from qualified investors that have accounts, and custody their funds and securities, with U.S. registered broker-dealers. Because we expect that qualified investors would likely select a foreign broker-dealer for its knowledge of local markets and/or its ability to execute trades in particular markets, as they would under Exemption (A)(*1*), but the foreign broker-dealer would not be acting as custodian of the funds and securities of the qualified investor (*i.e.,* not acting as a full-service broker), we do not believe it would be necessary for Exemption (A)(*2*) to include certain of the requirements proposed to be included in Exemption (A)(*1*), particularly the proposed requirement that the foreign broker-dealer conduct a foreign business, as described above.

i. Role of the U.S. Registered Broker-Dealer

Under Exemption (A)(*2*), the U.S. registered broker-dealer would be responsible for maintaining books and

[97] *See* Exchange Act Section 2, 15 U.S.C. 78b.

[98] *See* Exchange Act Section 3(f); *see also* Part VI.C., *infra*.

[99] *See* proposed Rule 15a–6(b)(5).

[100] *See* proposed Rule 15a–6(b)(3).

records, including copies of all confirmations issued by the foreign broker-dealer to the qualified investor, relating to any transactions effected under this exemption.[101] This requirement is designed to ensure that the Commission would have access to books and records relating to resulting transactions, as well as copies of confirmations issued by the foreign broker-dealer to the qualified investor. Because the U.S. registered broker-dealer would carry the account of the qualified investor under Exemption (A)(*2*), we understand from discussions with industry representatives that it would be consistent with current business practices for the U.S. registered broker-dealer to maintain the books and records for transactions effected under this exemption.

Proposed Exemption (A)(*2*) would also require the U.S. registered broker-dealer to receive, deliver and safeguard funds and securities in connection with the transactions on behalf of the qualified investor in compliance with Rule 15c3–3 under the Exchange Act.[102] As explained below, Exemption (A)(*2*) is designed to permit qualified investors that have an account with a U.S. registered broker-dealer to have access to foreign broker-dealers regardless of the types of securities that are involved.[103]

Unlike under the current rule, under Exemption (A)(*2*), the intermediating U.S. registered broker-dealer would not be required to effect the transaction.[104] Thus, with respect to transactions effected pursuant to Exemption (A)(*2*), the intermediating U.S. registered broker-dealer would no longer be required to comply with the provisions of the federal securities laws, the rules thereunder and SRO rules applicable to a broker-dealer effecting a transaction in securities, unless it were otherwise involved in effecting the transaction.[105] However, if a foreign broker-dealer effects a transaction pursuant to Exemption (A)(*2*) on a U.S. national securities exchange, through a U.S. alternative trading system, or with a market maker or an over-the-counter dealer in the United States, as is common with respect to U.S. securities, a U.S. registered broker-dealer would be involved in effecting the transaction and would be required to comply with the provisions of the federal securities laws, the rules thereunder and SRO rules applicable to such activity. In other words, such provisions would apply with respect to all transactions in U.S. securities under Exemption (A)(*2*) other than certain over-the-counter transactions that a foreign broker-dealer does not effect by or through a U.S. registered broker-dealer.

ii. Role of the Foreign Broker-Dealer

A foreign broker-dealer relying on Exemption (A)(*2*) would not be permitted to maintain custody of qualified investor funds and securities relating to any resulting transactions. Because of this limitation, Exemption (A)(*2*) would be available to all foreign broker-dealers and not just those that conduct a foreign business. Because entities that meet the definition of foreign broker-dealer under the proposed rule could not operate full-service brokerage under this exception, we believe that there is less risk of regulatory arbitrage.

Like Exemption (A)(*1*), Exemption (A)(*2*) would only be available to foreign broker-dealers that are regulated for conducting securities activities, including the specific activities in which the foreign broker-dealer engages with the qualified investor, in a foreign country by a foreign securities authority.[106] This requirement is designed to ensure that only foreign entities that are legitimately in the business of conducting securities activities (such as effecting transactions in securities), and that are regulated in the conduct of those activities, could rely on Exemption (A)(*2*). In addition, the foreign broker-dealer relying on Exemption (A)(*2*) would be required to disclose to the qualified investor that the foreign broker-dealer is regulated by a foreign securities authority and not by the Commission. Unlike under Exemption (A)(*1*), however, the foreign broker-dealer relying on Exemption (A)(*2*) would not be required to provide disclosures to the qualified investor regarding segregation requirements, bankruptcy protections and protections under SIPA. The Commission does not believe these disclosures would be necessary given that, under proposed Exemption (A)(*2*), the U.S. registered broker-dealer would be maintaining custody of funds and securities of qualified investors in connection with the resulting transactions.

As noted above, we expect that Exemption (A)(*2*) would be used by qualified investors that would like to access foreign broker-dealers but nonetheless would like to have an account, and maintain custody of their funds and securities, with a U.S. registered broker-dealer. Because a foreign broker-dealer would be selected for its knowledge of local markets and/or its ability to execute trades in particular markets, but would not be acting as custodian of the funds and securities of the qualified investor (*i.e.*, not acting as a full-service broker), we do not believe it would be necessary for proposed Exemption (A)(*2*) to include certain of the requirements contained in proposed Exemption (A)(*1*), particularly the requirement that the foreign broker-dealer conduct a foreign business, as described above.

The Commission requests comment on proposed Exemption (A)(*2*) generally. How would this exemption likely be used and by whom? Should proposed Exemption (A)(*2*) be available when the U.S. registered broker-dealer does not maintain custody of the qualified investor's funds and securities (*e.g.*, when a U.S. or foreign affiliate of the U.S. registered broker-dealer custodies the funds and securities otherwise than pursuant to Rule 15c3–3 under the Exchange Act)?[107]

The Commission also seeks comment on whether the proposed rule should require the U.S. registered broker-dealer to comply with any requirements with respect to transactions under Exemption (A)(*2*) other than the proposed requirement to maintain books and records and maintain custody of qualified investors' funds and securities relating to the transactions. Should the requirements differ based on whether the securities are U.S. securities or foreign securities? If so, why?

In addition, the Commission seeks comment on whether the proposed disclosures would provide appropriate notice to qualified investors that foreign broker-dealers would not be subject to the same regulatory requirements as U.S. registered broker-dealers. Would notice be sufficient? Are there are other

[101] *See* proposed Rule 15a–6(a)(3)(iii)(A)(*2*)(*i*).

[102] 17 CFR 240.15c3–3. *See* proposed Rule 15a–6(a)(3)(iii)(A)(*2*)(*ii*). Securities received and safeguarded under Exemption (A)(*2*) would be securities carried for the account of a customer under Rule 15c3–3(a)(2). 17 CFR 240.15c3–3(a)(2).

[103] Under Exemption (A)(*2*), the foreign broker-dealer would be permitted to clear and settle the transactions on behalf of the U.S. registered broker-dealer. The Commission believes that this is appropriate for transactions effected under Exemption (A)(*2*) for investors that possess the sophistication of qualified investors, particularly given that the exemption would require a U.S. registered broker-dealer to maintain books and records and receive, deliver and safeguard funds and securities in connection with the transactions.

[104] *See* 17 CFR 240.15a–6(a)(3)(iii)(A) (requiring the U.S. registered broker-dealer to effect all aspects of a transaction other than negotiation of its terms) and proposed Rule 15a–6(a)(3)(iii)(A)(*2*); *see also* note 28, *supra*, for a discussion of the differing treatment of U.S. and foreign securities under current Rule 15a–6(a)(3)(iii)(A)(*1*).

[105] *See* note 28, *supra*, for a discussion of the differing treatment of U.S. and foreign securities under current Rule 15a–6(a)(3)(iii)(A)(*1*).

[106] *See* proposed Rule 15a–6(b)(2)(i).

[107] 17 CFR 240.15c3–3.

disclosures that should be required? In particular, should the foreign broker-dealer be required to identify the foreign securities authority or authorities regulating the foreign broker-dealer? Should disclosure of the applicable dispute resolution system be required? In addition, the Commission requests comment regarding the proposed required form of these disclosures. Should the proposed disclosures be eliminated or modified in any way? If so, how and why?

In general, the Commission seeks comment on whether proposed Exemption (A)(*1*) and Exemption (A)(*2*) alternatives would provide a meaningful choice for qualified investors wishing to access foreign broker-dealers. What would be the advantages and disadvantages of using each alternative?

2. Sales Activities

Both proposed Exemption (A)(*1*) and proposed Exemption (A)(*2*) would eliminate the requirements in current Rule 15a–6(a)(3) for foreign associated persons [108] to be accompanied by an associated person of a U.S. registered broker-dealer during in-person visits with U.S. investors. The proposed rule also would eliminate the current requirement for an associated person of a U.S. registered broker-dealer to participate in communications between foreign associated persons and U.S. investors, whether oral or electronic.

From discussions with industry representatives, the staff understands that the current chaperoning requirements have been criticized as impractical and that they have been viewed as imposing unnecessary operational and compliance burdens particularly for communications with broker-dealers in time zones outside those of the United States. The current rule allows some unchaperoned contacts, in part due to the existence of other provisions of the rule that require review of ''the background of, foreign personnel who will contact U.S. institutional investors.'' [109] The proposed amendments would retain the requirement that the background of foreign personnel be reviewed, albeit by the foreign broker-dealer,[110] but would expand the ability of foreign broker-dealers to have unchaperoned contacts. Specifically, the proposed rule would not limit a foreign broker-dealer's ability to have unchaperoned communications, both oral and electronic, with qualified investors, as part of a transaction pursuant to either exemption in paragraph (a)(3) of the proposed rule. In addition, the proposed rule would provide that a foreign associated person may conduct unchaperoned visits to qualified investors within the United States, provided that transactions in any securities discussed during visits by the foreign associated person with qualified investors are effected pursuant to either exemption in paragraph (a)(3) of the proposed rule because these transactions would be viewed as being solicited.[111] The Commission believes that increasing the ability of foreign broker-dealers to have unchaperoned contacts should provide greater flexibility for both investors and industry participants in conducting communications and that eliminating the requirement to have a U.S. registered broker-dealer present for such communications should not result in any significant loss of safeguards for qualified investors because of the sophistication and experience standards in the definition of qualified investor and the proposed disclosure requirements in Exemption (A)(*1*) and Exemption (A)(*2*).

As noted above, the proposed rule would allow a foreign broker-dealer to have unchaperoned visits within the United States. Whether a foreign associated person's stay in the United States would qualify as a ''visit'' for purposes of the proposed rule would be a facts and circumstances determination based on factors including, but not limited to, the purpose, length and frequency of any stays. The Commission proposes to interpret a ''visit'' as one or more trips to the United States over a calendar year that do not last more than 180 days in the aggregate. The purpose of this proposed limitation regarding visits is to prevent foreign broker-dealers from essentially having a permanent sales force in the United States, which may result in foreign broker-dealers essentially conducting a U.S. based business, similar to U.S. registered broker-dealers, without appropriate regulatory oversight of these foreign broker-dealers. We preliminarily believe that 180 days strikes the proper balance between facilitating legitimate foreign broker-dealer activity in the United States, such as investment banking, and the potential competitive issues with U.S. registered broker-dealers and investor protection concerns.

The Commission requests comment on its proposed interpretation of what would constitute a visit. Should the Commission provide a bright-line definition of what constitutes a ''visit'' or is a more flexible approach appropriate? Is it appropriate to interpret ''visit'' as a specific number of days in a calendar year that a foreign broker-dealer could be in the United States? If so, is 180 days a calendar year appropriate? Or would a lower number such as 120, 90, 60, or 30 days a calendar year be more appropriate? We also solicit comment on the factors for determining what qualifies as a ''visit,'' described above. In addition, the Commission requests comment on eliminating the chaperoning requirements of the current rule. Are unchaperoned contacts between foreign broker-dealers and their associated persons and qualified investors appropriate?

3. Establishment of Qualification Standards

Foreign broker-dealers intending to rely on proposed Rule 15a–6(a)(3) would need to meet certain qualification requirements.[112] As under the current rule, the foreign broker-dealer would be required to provide the Commission, upon request or pursuant to agreement between the Commission or the United States and any foreign securities authority, information or documents related to the foreign broker-dealer's activities in inducing or attempting to induce securities transactions by qualified investors.[113] This information would permit the Commission to monitor and follow up on transactional activity conducted under Rule 15a–6, as necessary and appropriate.

The proposed rule also would require the foreign broker-dealer to determine that its associated persons that effect transactions with qualified investors are not subject to a statutory disqualification under Section 3(a)(39) of the Exchange Act.[114] This would be a change from the current rule, which requires the U.S. registered broker-dealer intermediating the transaction to make this determination.[115] Specifically, current Rule 15a–6(a)(3)(ii)(B) requires a U.S. registered broker-dealer to determine that the foreign associated persons of a foreign broker-dealer effecting transactions with U.S. institutional investors or major U.S. institutional investors are not subject to

[108] The proposed rule would retain the definition of ''foreign associated person'' that is in paragraph (b)(2) of the current Rule 15a–6, but would substitute ''qualified investor'' for ''U.S. institutional investor or major U.S. institutional investor'' in the definition. *See* proposed Rule 15a–6(b)(1).

[109] *See* 1988 Proposing Release, 53 FR at 23653.

[110] *See* Proposed Rule 15a–6(a)(3)(i)(B) and (C).

[111] *See* proposed Rule 15a–6(a)(3)(ii).

[112] *See* proposed Rule 15a–6(a)(3)(i).

[113] *See* proposed Rule 15a–6(a)(3)(i)(A) and 17 CFR 240.15a–6(a)(3)(i)(B).

[114] *See* proposed Rule 15a–6(a)(3)(i)(B).

[115] *See* 17 CFR 240.15a–6(a)(3)(ii)(B).

a statutory disqualification specified in Section 3(a)(39) of the Exchange Act, or certain substantially equivalent foreign disciplinary actions. Because of subsequent legislation, the proposed rule would no longer separately describe the foreign equivalents of statutory disqualification.[116] The Commission believes shifting the responsibility for making the statutory disqualification determination would be appropriate because the foreign broker-dealer is in possession of the relevant information regarding its foreign associated persons. Thus, we believe, as a practical matter, foreign broker-dealers are already making this determination so that U.S. registered broker-dealers can comply with their obligations under the existing rule. As discussed below, the proposed rule would require the U.S. registered broker-dealer to obtain a representation from the foreign broker-dealer that it has made this determination.

Under the current rule, a U.S. registered broker-dealer must obtain, with respect to each foreign associated person, information specified in Rule 17a–3(a)(12) under the Exchange Act [117] that relates to activities under paragraph (a)(3).[118] The proposed rule would require the foreign broker-dealer to maintain this information in its files and make it available upon request by the U.S. registered broker-dealer or the Commission.[119] This information would include the foreign associated person's name; address; social security number or foreign equivalent; the starting date of employment or other association with the foreign broker-dealer; date of birth; a complete, consecutive statement of all the foreign associated person's business connections for at least the preceding ten years, including whether the employment was part-time or full-time; a record of any denial of membership or registration, and of any disciplinary action taken, or sanction imposed, upon the foreign associated person by any agency, or by any securities exchange or securities association, including any finding that the foreign associated person was a cause of any disciplinary action or had violated any law; a record of any denial, suspension, expulsion or revocation of membership or registration of any foreign broker-dealer with which the foreign associated person was associated in any capacity when such action was taken; a record of any permanent or temporary injunction entered against the foreign associated person or any foreign broker-dealer with which the foreign associated person was associated in any capacity at the time such injunction was entered; a record of any arrest or indictment for any felony or foreign equivalent, or any misdemeanor or foreign equivalent pertaining to securities, commodities, banking, insurance or real estate (including, but not limited to, acting or being associated with a foreign broker-dealer), fraud, false statements or omissions, wrongful taking of property or bribery, forgery, counterfeiting or extortion, and the disposition of the foregoing; and a record of any other name or names by which the foreign associated person has been known or which the foreign associated person has used.[120]

The proposed rule would provide that the information kept by the foreign broker-dealer as specified in Rule 17a–3(a)(12)(i)(D) [121] must include documentation of sanctions imposed by foreign securities authorities, foreign exchanges, or foreign associations, including without limitation those described in Section 3(a)(39) of the Exchange Act.[122] The Commission believes shifting the responsibility would be appropriate because the foreign broker-dealer is in possession of the relevant information regarding its foreign associated persons. Thus, we believe, as a practical matter, foreign broker-dealers are already making this determination so that U.S. registered broker-dealers can comply with their obligations under the existing rule. As discussed below, the proposed rule would require the U.S. registered broker-dealer to obtain a representation from the foreign broker-dealer that it is maintaining the required information.

Consistent with the current rule, proposed Rule 15a–6(a)(3) would require the U.S. registered broker-dealer to obtain from the foreign broker-dealer and each foreign associated person written consent to service of process for any civil action brought by or proceeding before the Commission or a self-regulatory organization (as defined in Section 3(a)(26) of the Exchange Act).[123] The U.S. registered broker-dealer would also be responsible for obtaining from the foreign broker-dealer a representation that the foreign broker-dealer has determined that any foreign associated person of the foreign broker-dealer effecting transactions with the qualified investor is not subject to a statutory disqualification specified in Section 3(a)(39) of the Act, as required by paragraph (a)(3)(i)(B) of the proposed rule and discussed above.[124]

In addition, the U.S. registered broker-dealer would be responsible for obtaining from the foreign broker-dealer a representation that it has in its files, and the foreign broker-dealer would make available upon request by the U.S. registered broker-dealer or the Commission, the types of information specified in Rule 17a–3(a)(12) under the Act, as required by paragraph (a)(3)(i)(C) of the proposed rule and discussed above.[125] Finally, the proposed rule would require the U.S. registered broker-dealer to maintain records of these written consents and representations and, as in the current rule, make these records available to the Commission upon request.[126] These proposed requirements are important because they are designed to ensure that the Commission would be able to obtain information regarding foreign associated persons if it were necessary in the context of an investigation into alleged misconduct by a foreign broker-dealer or persons associated with the foreign broker-dealer. The Commission believes that allowing U.S. registered broker-dealers to rely upon the determinations and representations of foreign broker-dealers discussed above is a balanced approach that should address the risks

[116] At the time the Commission adopted Rule 15a–6, the definition of ''statutory disqualification'' in Section 3(a)(39) did not include expulsions, suspensions or other orders under foreign statutes or foreign equivalents of U.S. regulatory authorities. The International Securities Enforcement Cooperation Act of 1990 amended Section 3(a)(39) to include certain foreign conduct and disciplinary action in the definition of ''statutory disqualification'', including each type of conduct or disciplinary action described in paragraphs (a)(3)(ii)(B)(*1*)(*i*)–(*v*), (a)(3)(ii)(B)(*2*) and (a)(*3*)(ii)(B)(*3*) of Rule 15a–6. *See* Pub. L. 101–550, 104 Stat. 2714 (1990).

[117] 17 CFR 240.17a–3(a)(12).

[118] *See* 17 CFR 240.15a–6(a)(3)(iii)(C).

[119] *See* Proposed Rule 15a–6(a)(3)(i)(C).

[120] 17 CFR 240.17a–3(a)(12).

[121] 17 CFR 240.17a–3(a)(12)(i)(D) (requiring a broker-dealer to make and keep current a record of any denial of membership or registration, and of any disciplinary action taken, or sanction imposed, upon the associated person by any federal or state agency, or by any national securities exchange or national securities association, including any finding that the associated person was a cause of any disciplinary action or had violated any law).

[122] *See* proposed Rule 15a–6(a)(3)(i)(C).

[123] *See* proposed Rule 15a–6(a)(3)(iii)(B) and 17 CFR 240.15a–6(a)(3)(iii)(C). As in the current rule, the consent would be required to provide that process may be served on them by service on the registered broker-dealer in the manner set forth on the registered broker's or dealer's current Form BD. This would put individuals on notice of the manner in which process would be served.

[124] *See* proposed Rule 15a–6(a)(3)(iii)(C).

[125] *See id.*

[126] *See* proposed Rule 15a–6(a)(3)(i)(D). The provisions of proposed Rules 15a–6(a)(3)(iii)(B) and (D) are similar to paragraphs (a)(3)(iii)(D) and (E) of the current rule, although the proposed rule would eliminate the requirement under current Rule 15a–6(a)(3)(iii)(E) that the registered broker-dealer maintain a written record of all records in connection with trading activities of the qualified investor involving the foreign broker-dealer. This requirement is subsumed in other sections of the proposed rule. *See* proposed Rule 15a–6(a)(3)(iii)(A)–(D).

to qualified investors related to, among other things, contacts with foreign associated persons with a disciplinary history.

The Commission seeks comment on the qualification standards that would apply to foreign broker-dealers and U.S. registered broker-dealers under the proposed rule. Commenters are invited to discuss whether reliance by a U.S. registered broker-dealer upon the determinations and representations of a foreign broker-dealer appropriately addresses the potential risks to qualified investors related to, among other things, contacts with foreign associated persons with a disciplinary history. Should any of the responsibilities for making the statutory disqualification determinations or obtaining consents be shifted? Should the proposed rule require that the foreign broker-dealer (or the U.S. registered broker-dealer) determine whether the foreign associated persons are subject to statutory disqualifications?

E. Counterparties and Specific Customers

As in the current rule, proposed Rule 15a–6(a)(4) would provide exemptions for foreign broker-dealers that effect transactions in securities with or for, or induce or attempt to induce the purchase or sale of any security, by certain persons, including registered broker-dealers, certain international banks and bank organizations, certain foreign persons temporarily present in the United States and certain U.S. persons or groups of U.S. persons abroad. We understand from discussions with industry that these exemptions have been workable for both foreign broker-dealers and the U.S. entities and we have no knowledge of investor protection concerns being raised. Accordingly, we do not propose to amend them.

We do, however, propose to provide an additional exemption for transactions with U.S. resident fiduciaries of accounts for ''foreign resident clients'' because it is our understanding that foreign resident clients would not assume that the broker-dealer through which a U.S. resident fiduciary is effecting transactions is regulated by the Commission.[127] The proposed rule would define ''foreign resident client'' to mean ''(i) any entity not organized or incorporated under the laws of the United States and not engaged in a trade or business in the United States for federal income tax purposes; (ii) any natural person not a resident for federal income tax purposes; and (iii) any entity not organized or incorporated under the laws of the United States, 85 percent or more of whose outstanding voting securities are beneficially owned by persons in subparagraphs (i) and (ii) of this paragraph.'' [128] Discussions with industry have indicated that these are the types of entities that would likely use the proposed exemption. We selected the 85 percent threshold to capture foreign entities that are predominantly foreign-owned, while accommodating a small amount of U.S. ownership.[129]

For purposes of both the broker-dealer registration provisions of the Exchange Act and the proposed exemption provided by Rule 15a–6(a)(4)(vi), a U.S. resident fiduciary is considered to be a U.S. person, regardless of the residence of the owners of the underlying accounts. Accordingly, absent an exemption, a foreign broker-dealer that induces or attempts to induce a securities transaction with a U.S. resident fiduciary would be required either to register with the Commission or effect transactions in accordance with Rule 15a–6(a)(3). We understand, however, that foreign resident clients of a U.S. resident fiduciary reasonably may not expect the U.S. broker-dealer regulatory requirements to apply to their transactions in foreign securities, in large part simply because the transactions are in foreign securities.

Accordingly, the proposed rule would permit a foreign broker-dealer to effect transactions in, or induce or attempt to induce the purchase or sale of, securities, with or for any U.S. person, other than a registered broker-dealer or a bank acting pursuant to an exception or exemption from the definition of ''broker'' or ''dealer,'' [130] that acts in a fiduciary capacity for an account of a foreign resident client. Consistent with our understanding of the expectations of foreign resident clients of a U.S. resident fiduciary, this proposed exemption would be available only to a foreign broker-dealer that conducts a foreign business.[131] As indicated above, this exemption would recognize that foreign resident clients would not expect that the broker-dealer through which a U.S. resident fiduciary is effecting transactions is regulated by the Commission. Moreover, under the proposed rule, the foreign broker-dealer would be required to obtain a written representation from the U.S. fiduciary that the account is managed in a fiduciary capacity for a foreign resident client.[132] This requirement is designed to ensure that the U.S. fiduciary is actually managing accounts for foreign resident clients.

The Commission seeks comment generally on the exemptions in paragraph (a)(4) of the proposed rule for transactions with certain U.S. entities. Are there entities or other categories of entities that should be included? The Commission particularly seeks comment on the proposed exemption for transactions with U.S. fiduciaries of accounts for foreign resident clients. Is the requirement that a foreign broker-dealer conduct a foreign business necessary or appropriate? Should the rule apply to U.S. fiduciaries for accounts other than those of foreign resident clients? The Commission requests comment on the definition of ''foreign resident client,'' in general, and the 85 percent foreign ownership threshold for entities not organized or incorporated under the laws of the United States, in particular. Should it be raised or lowered to better protect against regulatory arbitrage or to achieve its stated purposes? Commenters suggesting a different threshold or a different method for determining compliance with the threshold should explain why they would choose that threshold or method.

F. Familiarization With Foreign Options Exchanges

Over the years, foreign options exchanges have inquired regarding the

[127] *Cf.* Letter from Catherine McGuire, Chief Counsel, Division of Market Regulation, to Giovanni P. Prezioso, Cleary Gottlieb, Steen & Hamilton (Jan. 30, 1996).

[128] *See* proposed Rule 15a–6(b)(4).

[129] The Commission considers a person to be a control person if he or she directly or indirectly has the power to vote 25 percent or more of the voting securities or interests of an entity. *See, e.g.*, 17 CFR 240.12b–2. The concept of control, which is found in all the statutes administered by the Commission, varies to some degree between statutes. Although the Exchange Act does not define ''control,'' Rule 12b–2 under the Exchange Act defines ''control'' as ''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.'' This definition has been found to apply to all Exchange Act control determinations. *In re Commonwealth Oil / Tesoro Petroleum Securities Litigation*, 484 F. Supp. 253, 268 (W.D. Tex. 1979) (the right to vote 25 percent or more of the voting securities or is entitled to 25 percent or more of the profits is presumed to control that company). The 85 percent threshold in proposed paragraph (b)(4)(iii) is designed to ensure that entities with U.S. control persons would not meet the proposed definition of ''foreign resident client.''

[130] *See* Sections 3(a)(4)(B), 3(a)(4)(E) and 3(a)(5)(C) of the Exchange Act. Foreign broker-dealers that want to effect transactions for registered broker-dealers or banks acting pursuant to certain exceptions or exemptions from the definition of ''broker'' or ''dealer'' can do so under the exemption in paragraph (a)(4)(i) of Rule 15a–6. *See* 17 CFR 240.15a–6(a)(4)(i).

[131] *See* proposed Rule 15a–6(b)(2)(ii).

[132] *See* proposed Rule 15a–6(a)(4)(vi)(B).

permissibility of limited activities designed to familiarize U.S. entities that have had prior actual experience with traded options in U.S. options markets, such as U.S. registered broker-dealers and certain U.S. institutional investors, with the existence and operations of, and options on foreign securities traded on, such foreign options exchanges. These exchanges have limited the activities conducted by their representatives, who may be located in a foreign office or in a representative office in the United States, and by their foreign broker-dealer members.

1. Exchange Act Section 15(a)

Because the activities by a representative of a foreign options exchange may constitute solicitation,[133] they raise potential registration concerns for foreign broker-dealer participants on the exchanges under Section 15(a).[134] This is in part because the activities are undertaken with the expectation that one or more U.S. registered broker-dealers or U.S. institutional investors will engage in foreign options transactions executed through the exchange, and thus trade through one or more foreign broker-dealer members of the exchange. Similarly, the activities of a foreign broker-dealer member of a foreign options exchange may constitute solicitation under the Commission's broad interpretation of solicitation.

The Commission recognizes the role of these activities in making certain U.S. investors aware of foreign options markets and the options on foreign securities traded on those markets. Accordingly, the Commission is proposing a new exemption to provide legal certainty for the foreign broker-dealer members and these foreign options exchanges. Paragraph (a)(5) of proposed Rule 15a–6 would allow a foreign broker-dealer that is a member of a foreign options exchange to effect transactions in options on foreign securities listed on that exchange for a qualified investor that has not otherwise been solicited by the foreign broker-dealer.[135] Under this exemption, a foreign broker-dealer, a foreign options exchange and representatives of the foreign options exchange could conduct certain activities or communicate with a qualified investor in a manner that might otherwise be considered a form of solicitation, as described below.[136] Transactions effected by or through the foreign broker-dealer with or for qualified investors that result from these activities or communications would not require registration or compliance with proposed Rule 15a–6(a)(3). However, while these activities would not necessarily constitute a form of solicitation, the Commission anticipates that given the broad interpretation of solicitation, it would be difficult, if not impractical, to conduct repeated transactions with the same qualified investor without the foreign broker-dealer engaging in some form of communication that would constitute solicitation. Therefore, the Commission anticipates that most transactions with qualified investors resulting from these activities or communications would need to be completed pursuant to proposed Rules 15a–6(a)(3).

Paragraph (a)(5)(i) of proposed Rule 15a–6 would set forth the limited activities in which a representative of a foreign options exchange located in a foreign office or a representative office in the United States may engage vis-à-vis qualified investors. The proposed rule would allow the representative of a foreign options exchange to communicate with persons that he or she reasonably believes are qualified investors regarding the foreign options exchange, the options on foreign securities traded on the foreign options exchange, and, if applicable, the foreign options exchange's ''OTC options processing service,'' as defined below.[137] Such communications could include programs and seminars in the United States.

Proposed Rule 15a–6(b)(6) would define an ''OTC options processing service'' as ''a mechanism for submitting an options contract on a foreign security that has been negotiated and completed in an over-the-counter transaction to a foreign options exchange so that the foreign options exchange may replace that contract with an equivalent standardized options contract that is listed on the foreign options exchange and that has the same terms and conditions as the over-the-counter options.'' By utilizing an OTC options processing service, qualified investors would be able to take advantage of the flexible nature of the OTC options market, while realizing certain efficiencies and benefits available in an exchange-traded market. In particular, qualified investors would have greater opportunities to close out options positions. In a typical OTC options transaction, a party must either negotiate with its counterparty to close out the trade or enter into an offsetting transaction to reduce its risk. In addition, OTC options processing services would provide a means for qualified investors to reduce other risks that arise in trading in the OTC options market, including credit risks, liquidity risks, legal risks and operational risks. By using an OTC options processing service, qualified investors would be able to access the benefits available in the OTC options market while taking advantage of the benefits and decreased risks available in the exchange-traded market.

The proposed rule would also permit a representative of a foreign options exchange to provide persons that the representative of the foreign options exchange reasonably believes are qualified investors with a disclosure document that provides an overview of the foreign options exchange and the options on foreign securities traded on that exchange, including the differences from standardized options in the U.S. options market and special factors relevant to transactions by U.S. entities in options on the foreign options exchange.[138] In addition, a representative of a foreign options exchange could make available to persons that the representative of the foreign options exchange reasonably believes are qualified investors, solely upon the request of the investor, a list of participants on the foreign options exchange permitted to take orders from the public and any U.S. registered broker-dealer affiliates of such participants.[139] Moreover, paragraph (5)(iii) would allow the foreign exchange to make available to qualified investors, through the foreign broker-dealer, the exchange's OTC options processing service.[140]

In proposing to limit these activities, the proposed rule is designed to ensure that a foreign options exchange and its representatives do not engage in solicitation on behalf of a particular foreign broker-dealer or limited group of particular foreign broker-dealers.

Paragraph (a)(5)(ii) of the proposed rule would set forth the activities in which a foreign broker-dealer could engage in connection with transactions effected on a foreign options exchange

[133] For a discussion of the Commission's broad interpretation of solicitation, *see* Parts II.A. and III.B., *supra*.

[134] The fact that the activities are conducted by the exchanges through their representatives does not necessarily eliminate the registration concerns of the participants on those exchanges. *See* Exchange Act Section 20(b), 17 U.S.C. 78t(b) (''It shall be unlawful for any person, directly or indirectly, to do any act or thing which it would be unlawful for such person to do under the provisions of this title or any rule or regulation thereunder through or by means of any other person'').

[135] *See* proposed Rule 15a–6(a)(5).

[136] *See* proposed Rules 15a–6(a)(5)(i)–(iii).

[137] *See* proposed Rule 15a–6(a)(5)(i)(A).

[138] *See* proposed Rule 15a–6(a)(5)(i)(B).

[139] *See* proposed Rule 15a–6(a)(5)(i)(C).

[140] *See* proposed Rule 15a–6(a)(5)(iii).

of which it is a member. A foreign broker-dealer would be permitted to make available to qualified investors the foreign options exchange's OTC options processing service.[141] A foreign broker-dealer would also be permitted to provide qualified investors, in response to an otherwise unsolicited inquiry concerning foreign options traded on the foreign options exchange, with a disclosure document that provides an overview of the foreign options exchange and the options on foreign securities traded on that exchange, including the differences from standardized options in the U.S. domestic options market and special factors relevant to transactions by U.S. entities in options on that exchange.[142]

2. Exchange Act Sections 5 and 6

Section 5 of the Exchange Act makes it ''unlawful for any broker, dealer, or exchange, directly or indirectly, to make use of the mails or any means or instrumentality of interstate commerce for the purpose of using any facility of an exchange with or subject to the jurisdiction of the United States to effect any transaction in a security, or to report any such transaction,'' unless such exchange is registered under Section 6 of the Exchange Act or exempt from such registration.[143] As described above, paragraph (a)(5) of proposed Rule 15a–6 would establish the limited activities and communications in which a representative of a foreign options exchange located in a foreign office or a representative office in the United States may engage vis-à-vis qualified investors,[144] and in which a foreign broker-dealer may engage in connection with transactions effected on a foreign options exchange in which it is a member.[145] In addition, a foreign exchange could make available to qualified investors, through a foreign broker-dealer, the exchange's OTC options processing service.[146]

The Commission is proposing to provide interpretive guidance that a foreign exchange would not be required to register as a national securities exchange under Section 6 of the Exchange Act or be exempt from such registration if the foreign exchange, its representatives, or its foreign broker-dealer members engaged in the limited activities and communications described in proposed paragraph (a)(5) of Rule 15a–6. The Commission's proposed interpretation is based on its preliminary view that, although a foreign exchange's OTC options processing service may be a facility of an exchange,[147] the OTC options processing service would not effect any transaction in a security or report any such transaction.[148] Accordingly, such activity would not trigger the registration requirements of Section 6 of the Exchange Act.[149]

The Commission seeks comment on its proposed interpretation that a foreign exchange would not be required to register as a national securities exchange under Section 6 of the Exchange Act if the foreign exchange, its representatives, or its foreign broker-dealer members engage in the limited activities and communications described in paragraph (a)(5) of proposed Rule 15a–6. Are any additional conditions necessary or are there other interpretive issues relating to the circumstances under which a foreign exchange would be required to register under Section 6 of the Exchange Act, or otherwise obtain an exemption from such registration requirements, that the Commission should address?

3. Exchange Act Section 17A

Under proposed Rule 15a–6(a)(5), qualified investors would not become direct members of, or participants in, the foreign options exchange or any associated foreign clearing organization. Further, the foreign options exchange would not trade nor would the foreign clearing organization clear and settle options on U.S. securities for a foreign broker-dealer member or participant relying on proposed paragraph (a)(5) for the transaction. The foreign broker-dealer member or participant would execute transactions in options on foreign securities, or submit an options contract on foreign securities, and the foreign clearing organization would clear and settle these transactions for its foreign broker-dealer participants in the same manner as any other transaction executed on the foreign options exchange.

Section 17A(b)(1) of the Exchange Act prohibits any clearing agency from directly or indirectly making ''use of the mails or any means or instrumentality of interstate commerce to perform the functions of a clearing agency with respect to any security (other than an exempted security),'' unless it is registered with the Commission.[150] The Commission may conditionally or unconditionally exempt any clearing agency if the Commission finds that such exemption is consistent with the public interest, the protection of investors and the purposes of Section 17A.[151]

Previously, the Commission has required foreign clearing organizations to obtain an exemption from clearing agency registration only when the foreign clearing organization provides clearance and settlement services for U.S. securities directly to U.S. entities. For example, the Commission granted Euroclear and Clearstream (formerly Cedel Bank) exemptions from clearing agency registration in order that they could provide clearance and settlement services for U.S. government securities to their U.S. participants.[152] Because only the foreign broker-dealer would have direct access to the foreign clearing organization to clear and settle foreign securities transactions under proposed Rule 15a–6(a)(5), the Commission does not believe that relief under Section 17A of the Exchange Act would be necessary. The Commission solicits comment on whether any interpretive guidance is needed under Section 17A with respect to activities under proposed Rule 15a–6(a)(5). If so, what?

4. Securities Act

Foreign option transactions that are effected through the facilities of a foreign exchange will generally involve the offer and sale of a security by an issuer of the security.[153] As a result,

[141] *See* proposed Rule 15a–6(a)(5)(ii)(A).

[142] *See* proposed Rule 15a–6(a)(5)(ii)(B). Exchange Act Rule 9b–1 requires an options market to file with the Commission an options disclosure document containing the information specified in Rule 19b–1(c). ''Options markets'' are defined in Rule 19b–1 to include foreign securities exchanges. *See* Exchange Act Rule 19b–1(a)(1), 17 CFR 240.19b–1(a)(1). The Commission would not view the provision of the options disclosure document, which contains, among other things, a summary of the instruments traded and the mechanics of trading on that market, as a ''research report'' under proposed Rule 15a–6(a)(2). *See* Parts II.B. and III.C., *supra*.

[143] 15 U.S.C. 78e.

[144] *See* proposed Rule 15a–6(a)(5)(i).

[145] *See* proposed Rule 15a–6(a)(5)(ii).

[146] *See* proposed Rule 15a–6(a)(5)(iii).

[147] *See* Section 3(a)(2) of the Exchange Act, 15 U.S.C. 78c(a)(2) (defining ''facility'' of an exchange).

[148] *See* note 143 and accompanying text, *supra* (discussing Section 5 of the Exchange Act, which prohibits a broker, dealer, or exchange from using a facility of an exchange to effect a transaction in a security, or to report any such transaction, unless such exchange is registered under Section 6 of the Exchange Act).

[149] *See* Section 3(a)(1) of the Exchange Act, 15 U.S.C. 78c (defining ''exchange'') and Rule 3b–16 under the Exchange Act, 17 CFR 240–3b–16 (further elaborating on the definition of ''exchange'' contained in the Exchange Act).

[150] 15 U.S.C. 78q–1(b)(1).

[151] *Id.*

[152] *See* Exchange Act Release Nos. 43775 (Dec. 28, 2000), 66 FR 819 (order exempting Euroclear Bank from clearing agency registration) and 39643 (Feb. 18, 1998), 63 FR 8232 (order exempting Euroclear Bank's predecessor, Morgan Guaranty Trust Company, as operator of the Euroclear system, from clearing agency registration) and Exchange Act Release No. 38328 (Feb. 24, 1997), 62 FR 9225 (order exempting Clearstream Bank, formerly Cedel Bank, from clearing agency registration).

[153] With exchange traded options, the clearing house is the issuer of the option security. *See*

unless the foreign options were registered under the Securities Act, foreign option transactions involving U.S. persons would be required to come within an exemption from registration. To the extent that the activities undertaken by foreign options exchange in the United States can be deemed to constitute offers of foreign options under the Securities Act, such activities must also be undertaken in a fashion that is consistent with the requirements of the applicable exemption.[154]

5. Request for Comment

The Commission seeks comment on the proposed exemption in paragraph (a)(5) for transactions effected by a foreign broker-dealer on a foreign options exchange of which it is a member. Should the Commission require a foreign broker-dealer or a representative of a foreign options exchange to determine that the persons with whom the representative communicates or otherwise provides information under proposed paragraphs (a)(5)(i)(A)–(C) are, in fact, qualified investors? Should the exemption be limited to unsolicited transactions? As a practical matter, because of the broad interpretation of solicitation, would foreign broker-dealers effecting transactions with qualified investors that have been approached by the representatives of a foreign options exchange effect these transactions in reliance on proposed paragraph (a)(3) of Rule 15(a)(6)? If not, should the proposed exemption permit foreign broker-dealers to engage in additional limited solicitation activities, such as the types of contacts that would be expected in an ongoing customer relationship? In general, should foreign representatives of foreign options exchanges or foreign options exchanges be permitted to engage in any other activities under the proposed rule? If so, what? Given the purpose of the exemption to allow familiarization activities for foreign options exchanges, are there other types of markets for which it would be appropriate to permit familiarization activities? If so, which markets and what should the permissible range of activities be? Should they be broader or narrower than the permissible range of activities for foreign options exchanges? If so, why? Commenters are requested to explain their views.

G. Scope of the Proposed Exemption

When we adopted Rule 15a–6 in 1989, the Commission had authority, under Section 15(a)(2) of the Exchange Act, only to conditionally or unconditionally exempt from the broker-dealer registration requirements of Section 15(a)(1) any broker-dealer or class of broker-dealers, by rule or order, as it deems consistent with the public interest and the protection of investors.[155] However, many of the statutory and regulatory provisions under the Exchange Act actually are applicable by their terms to broker-dealers regardless of their registration status.[156] To provide foreign broker-dealers relying on the exemptions in Rule 15a–6 with relief from these provisions, the Commission stated in the 1989 Adopting Release, ''Nevertheless, the staff would not recommend that the Commission take enforcement action against foreign broker-dealers for want of compliance with those provisions, with the exception of sections 15(b)(4) and 15(b)(6), if the foreign broker-dealers were exempt from broker-dealer registration under the Rule.'' [157]

Since 1996, the Commission has had general exemptive authority under Section 36 of the Exchange Act to conditionally or unconditionally exempt any person, security, or transaction, or any class or classes of persons, securities, or transactions, from any provision or provisions of the Exchange Act or any rule or regulation thereunder, by rule, regulation or order, to the extent that such exemption is necessary or appropriate in the public interest and is consistent with the protection of investors.[158]

The Commission proposes to amend Rule 15a–6 to exempt foreign broker-dealers from not only the registration requirements of Section 15(a)(1) or 15B(a)(1) of the Exchange Act, but also from the reporting and other requirements of the Exchange Act (other than Sections 15(b)(4) and 15(b)(6)), and the rules and regulations thereunder, that apply specifically to a broker-dealer solely by virtue of its status as a broker or dealer rather than because of its registration with the Commission.

Under the proposed rule, as under the current rule, however, foreign broker-dealers would not be exempt from provisions of the Exchange Act, and the rules and regulations thereunder, that are not specific to broker-dealers, such as Section 10(b) of the Exchange Act, or Rule 10b–5 thereunder.[159] Such rules apply to ''persons'' regardless of their registration status, and thus apply equally to registered broker-dealers, unregistered broker-dealers and non-broker-dealers. We also do not propose to exempt foreign broker-dealers from Exchange Act Sections 15(b)(4) and 15(b)(6), which give the Commission the authority to sanction broker-dealers and persons associated with broker-dealers, because these sections provide the Commission with flexibility to impose a bar against or place other limitations on associated persons or place limitations on broker-dealers in the circumstances specified in these sections.

As discussed more fully below with respect to each of the exemptions in the proposed rule, the Commission preliminarily believes that exempting foreign broker-dealers from the registration requirements of Sections 15(a)(1) and 15B(a)(1) of the Exchange Act and the reporting and other requirements of the Exchange Act (other than Sections 15(b)(4) and 15(b)(6)), and the rules and regulations thereunder, that apply specifically to a broker-dealer that is not registered with the Commission solely by virtue of its status as a broker or dealer would be necessary or appropriate in the public interest, and would be consistent with the protection of investors.

1. Proposed Rule 15a–6(a)(2)

As discussed above, proposed rule 15a–6(a)(2) would permit a foreign broker-dealer to provide research reports to qualified investors, but not otherwise induce or attempt to induce the purchase or sale of any security by qualified investors.[160] Based on conversations with industry participants, we understand that foreign broker-dealers rarely rely on current Rule 15a–6(a)(2). This is in part because of the limitations on solicitation, as well as the requirement that if a foreign broker-dealer has a relationship with a U.S. registered broker-dealer that satisfies the requirement of paragraph (a)(3) of the current rule, any

Securities Act Release No. 8171 (Dec. 23, 2002), 68 FR 188, 188 (Jan. 2, 2003).

[154] For example, to the extent that reliance is based on Securities Act Section 4(2), the activities of the foreign options exchange must not constitute a public offering of the securities.

[155] *See* 15 U.S.C. 78o(a)(2); *see also* Section 15B(a)(4) of the Exchange Act, 15 U.S.C. 78o–4(a)(4) (giving the Commission similar authority with respect to municipal securities dealers).

[156] *See* 1989 Adopting Release, 54 FR at 30015 n.22 (''*E.g.*, sections 15(b)(4) and 15(b)(6) of the Exchange Act, 15 U.S.C. 78o(b)(4) and 78o(b)(6); Rules 15c3–1, 15c3–3, 17a–3, 17a–4, and 17a–5, 17 CFR 240.15c3–1, 15c3–3, 17a–3, 17a–4, and 17a–5'').

[157] *See* 1989 Adopting Release, 54 FR at 30015 n.22.

[158] *See* 15 U.S.C. 78mm; *see also* Capital Markets Efficiency Act of 1996, Sec. 105(b), Pub. Law 104–290, 110 Stat. 3416 (1996) (adding Section 36 to the Exchange Act).

[159] The proposed rule also would not affect any obligations a foreign broker-dealer may have under any other law, including the Securities Act.

[160] *See* Part III.C., *supra*.

transactions with the foreign broker-dealer in securities discussed in the research reports must be effected pursuant to the provisions of paragraph (a)(3).[161]

Given the *de minimis* volume of transactions that likely would be conducted,[162] and the level of financial sophistication of the investors that could receive the research reports under this proposed exemption, as well as the fact that the foreign broker-dealer would not otherwise be permitted to induce or attempt to induce the purchase or sale of any security by those investors under the proposed exemption, the Commission preliminarily believes that it would be necessary or appropriate in the public interest, and would be consistent with the protection of investors, to exempt foreign broker-dealers relying on paragraph (a)(2) of the proposed rule from the registration requirements of Sections 15(a)(1) and 15B(a)(1) of the Exchange Act and the reporting and other requirements of the Exchange Act (other than Sections 15(b)(4) and 15(b)(6)), and the rules and regulations thereunder, that apply specifically to a broker-dealer that is not registered with the Commission solely by virtue of its status as a broker or dealer.

The Commission solicits comment on whether it would be necessary or appropriate in the public interest, and consistent with the protection of investors, to exempt foreign broker-dealers relying on paragraph (a)(2) of the proposed rule from such rules and requirements. If not, which provisions or rules should apply and why?

2. Proposed Rule 15a–6(a)(3)

a. Exemption (A)(*1*)

As discussed above, foreign broker-dealers relying on proposed Exemption (A)(*1*) under Rule 15a–6(a)(3) would be required to conduct a foreign business.[163] The proposed rule would define ''foreign business'' to mean the business of a foreign broker-dealer with qualified investors and foreign resident clients [164] where at least 85% of the aggregate value of the securities purchased or sold in transactions conducted pursuant to both paragraphs (a)(3) and (a)(4)(vi) of the proposed rule by the foreign broker-dealer, calculated on a rolling two-year basis, is derived from transactions in foreign securities, as defined above.[165] As explained above, the Commission believes that making Exemption (A)(*1*) available only to a foreign broker-dealer conducting a foreign business would provide U.S. investors increased access to foreign securities and markets without creating opportunities for regulatory arbitrage vis-à-vis U.S. securities markets because the foreign broker-dealer's business in U.S. securities would be limited.

Given the requirement that foreign broker-dealers conduct a foreign business and the sophistication of qualified investors, as well as the other investor protections in the proposed rule, the Commission preliminarily believes that it would be necessary or appropriate in the public interest, and would be consistent with the protection of investors to exempt foreign broker-dealers relying on Exemption (A)(*1*) of the proposed rule from the registration requirements of Sections 15(a)(1) and 15B(a)(1) of the Exchange Act and the reporting and other requirements of the Exchange Act (other than Sections 15(b)(4) and 15(b)(6)), and the rules and regulations thereunder, that apply specifically to a broker-dealer that is not registered with the Commission solely by virtue of its status as a broker or dealer.

The Commission solicits comment on whether it would be necessary or appropriate in the public interest, and consistent with the protection of investors, to exempt foreign broker-dealers relying on Exemption (A)(*1*) from such rules and requirements. If not, which rules should apply and why? Alternatively, and as under current Rule 15a–6(a)(3), should the intermediating U.S. registered broker-dealer be required to comply with certain rules in lieu of the foreign broker-dealer? If so, which rules and why? Should the requirements differ based on whether the securities are U.S. securities or foreign securities and where the transactions are executed? Would exempting foreign broker-dealers from such rules and regulations place U.S. registered broker-dealers at a competitive disadvantage?

b. Exemption (A)(*2*)

Under proposed Exemption (A)(*2*), qualified investors that have an account with a U.S. registered broker-dealer would have access to foreign broker-dealers regardless of the types of securities that are involved. Foreign broker-dealers relying on proposed Exemption (A)(*2*) would be permitted to effect transactions in securities, provided, among other things, that a U.S. registered broker-dealer acts as custodian for any resulting transactions.[166] As a result, a U.S. registered broker-dealer would hold the funds and securities of the qualified investor and be subject to the Commission's rules relating to the safeguarding of customer assets, such as Exchange Act Rule 15c3–3. As with proposed Exemption (A)(*1*), proposed Exemption (A)(*2*) would be limited to transactions with qualified investors, which we believe are sophisticated investors that can be expected to understand the risk of dealing with foreign broker-dealers that are not regulated by the Commission.

Given the requirement that a U.S. registered broker-dealer maintain custody of qualified investors' funds and securities from any resulting transactions and the sophistication of qualified investors, as well as the other investor protections in the proposed rule, the Commission preliminarily believes that it would be necessary or appropriate in the public interest, and would be consistent with the protection of investors, to exempt foreign broker-dealers relying on Exemption (A)(*2*) of the proposed rule from the registration requirements of Sections 15(a)(1) and 15B(a)(1) of the Exchange Act and the reporting and other requirements of the Exchange Act (other than Sections 15(b)(4) and 15(b)(6)), and the rules and regulations thereunder, that apply specifically to a broker-dealer that is not registered with the Commission solely by virtue of its status as a broker or dealer.

The Commission solicits comment on whether it would be necessary or appropriate in the public interest, and consistent with the protection of investors, to exempt foreign broker-dealers relying on Exemption (A)(*2*) from such rules and requirements. If not, which rules should apply and why? Alternatively, as under current Rule 15a–6(a)(3), should the intermediating U.S. registered broker-dealer be required to comply with certain rules in lieu of the foreign broker-dealer? If so, which rules and why? Should the requirements differ based on whether the securities are U.S. securities or foreign securities and where the transactions are executed? Would exempting foreign broker-dealers from such rules and regulations place U.S. registered broker-dealers at a competitive disadvantage?

3. Proposed Rule 15a–6(a)(4)

As explained above, paragraph (a)(4) of proposed Rule 15a–6 would provide an additional exemption for foreign broker-dealers that effect transactions

[161] *See* 17 CFR 240.15a–6(a)(2)(iii).

[162] This estimate is based on information the staff obtained in discussions with industry representatives.

[163] *See* Part III.D.1.a., *supra*.

[164] *See* Part III.E., *supra*.

[165] *See* proposed Rule 15a–6(b)(3).

[166] *See* Part III.D.1.b., *supra*.

for certain classes of investors, namely, U.S. persons that act in a fiduciary capacity for an account of a foreign resident client.[167]

Because of the nature and/or location of these persons, the Commission preliminarily believes that it would be necessary or appropriate in the public interest, and would be consistent with the protection of investors, to exempt foreign broker-dealers relying on paragraph (a)(4)(vi) of the proposed rule from the registration requirements of Sections 15(a)(1) and 15B(a)(1) of the Exchange Act and the reporting and other requirements of the Exchange Act (other than Sections 15(b)(4) and 15(b)(6)), and the rules and regulations thereunder, that apply specifically to a broker-dealer that is not registered with the Commission solely by virtue of its status as a broker or dealer.

The Commission solicits comment on whether it would be necessary or appropriate in the public interest, and be consistent with the protection of investors, to exempt foreign broker-dealers relying on paragraph (a)(4)(vi) of the proposed rule from such rules and requirements. If not, which rules should apply and why?

4. Proposed Rule 15a–6(a)(5)

As explained above, paragraph (a)(5) of proposed Rule 15a–6 would allow a foreign broker-dealer that is a member of a foreign options exchange to effect transactions in options on foreign securities listed on that exchange for a qualified investor that has not otherwise been solicited by the foreign broker-dealer.[168] Under this exemption, a foreign broker-dealer, a foreign options exchange and representatives of the foreign options exchange could conduct certain activities or communicate with a qualified investor in a manner that might otherwise be considered a form of solicitation, as described above.[169] Transactions effected by or through the foreign broker-dealer with or for qualified investors that result from these activities or communications would not require registration or, in some situations, compliance with proposed Rule 15a–6(a)(3). However, while these activities would not necessarily constitute a form of solicitation, the Commission anticipates that given the broad interpretation of solicitation, it would be difficult, if not impractical, to conduct repeated transactions with the same qualified investor without a foreign broker-dealer engaging in some form of communication that would constitute solicitation. Therefore, the Commission anticipates that most transactions with qualified investors resulting from these activities or communications would need to be completed pursuant to proposed Rules 15a–6(a)(3).

Hence, for the reasons given above in the discussion of paragraphs (a)(2) and (a)(3) of the proposed rule, the Commission preliminarily believes that it would be necessary or appropriate in the public interest, and would be consistent with the protection of investors to exempt foreign broker-dealers relying on paragraph (a)(5) of the proposed rule from the registration requirements of Sections 15(a)(1) and 15B(a)(1) of the Exchange Act and the reporting and other requirements of the Exchange Act (other than Sections 15(b)(4) and 15(b)(6)), and the rules and regulations thereunder, that apply specifically to a broker-dealer that is not registered with the Commission solely by virtue of its status as a broker or dealer.

The Commission solicits comment on whether it would be necessary or appropriate in the public interest, and be consistent with the protection of investors, to exempt foreign broker-dealers relying on paragraph (a)(5) of the proposed rule from such rules and requirements. If not, which rules should apply and why?

IV. Preliminary Findings

Section 15(a)(2) of the Exchange Act provides that the Commission, by rule or order, as it deems consistent with the public interest and the protection of investors, may conditionally or unconditionally exempt from Section 15(a)(1) any broker or dealer or class of brokers or dealers. Section 36 of the Exchange Act provides general exemptive authority to the Commission to exempt any person or class of persons or transactions from any provision of the Exchange Act, to the extent that such exemption is necessary or appropriate in the public interest and is consistent with the protection of investors. As described in Part III.G., above, the Commission preliminarily believes that the proposed exemptions would be necessary or appropriate in the public interest and would be consistent with the protection of investors.

V. General Request for Comment

In addition to the specific requests for comment above, the Commission seeks comment generally on all aspects of the proposed amendments to Rule 15a–6 under the Exchange Act. The Commission anticipates that all prior staff no-action relief under Rule 15a–6 would be superseded if the Commission were to adopt this proposed rule and interpretive guidance. Are there additional issues stemming from the 1989 Adopting Release or related staff guidance that are not addressed in the proposal and that should be addressed by this rule or interpretive guidance? Commenters are invited to provide empirical data to support their views. Comments are of the greatest assistance to our rulemaking initiatives if accompanied by supporting data and analysis of the issues addressed, and if accompanied by alternative suggestions to our proposals when appropriate. Commenters are also welcome to offer their views on any other issues raised by the proposed amendments to Rule 15a–6.

VI. Administrative Law Matters

A. Paperwork Reduction Act Analysis

Certain provisions of current Rule 15a–6 contain ''collection of information'' requirements within the meaning of the Paperwork Reduction Act of 1995.[170] The Commission has previously submitted these information collections to the Office of Management and Budget (''OMB'') for review in accordance with 44 U.S.C. 3507(d) and 5 CFR 1320.11. The revised collections of information in the proposed amendments would impose certain burdens on U.S. registered broker-dealers, foreign broker-dealers and U.S. persons acting as fiduciaries as described in proposed Rule 15a–6(a)(4)(vi). The Commission has submitted the revised collections of information, entitled ''Rule 15a–6 under the Securities Exchange Act of 1934—Exemption of Certain Foreign Brokers or Dealers'' (OMB control No. 3235–0371), to the OMB for review. 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.[171]

1. Related Collections of Information Under Proposed Paragraphs (a)(3)(i)(B) and (C) and (a)(3)(iii)(C) and (D)

Current paragraph (a)(3)(ii)(B) of Rule 15a–6 requires a U.S. registered broker-dealer to determine that the foreign associated persons of a foreign broker-dealer effecting transactions with U.S. institutional investors or major U.S. institutional investors are not subject to a statutory disqualification as defined in Section 3(a)(39) of the Exchange Act, or certain substantially equivalent foreign

[167] *See* Part III.E., *supra*.

[168] *See* Part III.F., *supra*.

[169] *See* proposed Rules 15a–6(a)(5)(i)–(iii).

[170] 44 U.S.C. 3501 *et seq*.

[171] *See* 44 U.S.C. 3512.

disciplinary actions. As described above, because the foreign equivalents of statutory disqualification are now included in Section 3(a)(39), the proposed rule would no longer separately describe them.[172] In addition, the proposed rule would place the burden on the foreign broker-dealer to determine that its foreign associated persons effecting transactions with a qualified investor are not subject to a statutory disqualification as defined in Section 3(a)(39) of the Exchange Act.[173]

Current paragraph (a)(3)(iii)(C) of Rule 15a–6 requires a U.S. registered broker-dealer to obtain from the foreign broker-dealer, with respect to each foreign associated person, the types of information specified in Rule 17a–3(a)(12) under the Exchange Act,[174] provided that the information required by paragraph (a)(12)(i)(D) of that rule includes sanctions imposed by foreign securities authorities, exchanges, or associations, including statutory disqualification.[175] Proposed paragraph (a)(3)(i)(C) of Rule 15a–6 would require that the foreign broker-dealer have such information regarding its foreign associated persons in its files.

Proposed paragraphs (a)(3)(iii)(C) and (D) of Rule 15a–6 would require that a registered broker-dealer obtain and record a representation from the foreign broker-dealer that the foreign broker-dealer has determined that its foreign associated persons effecting transactions with a qualified investor are not subject to a statutory disqualification as defined in Section 3(a)(39) of the Exchange Act and has the information required by proposed paragraph (a)(3)(i)(C) of Rule 15a–6 in its files.

a. Collection of Information

Proposed paragraphs (a)(3)(i)(B) and (C) and (a)(3)(iii)(C) and (D) of Rule 15a–6 all would require ''collections of information,'' as that term is defined in 44 U.S.C. 3502(3). Proposed paragraph (a)(3)(i)(B) would require a foreign broker-dealer to make a determination that its foreign associated persons effecting transactions with a qualified investor are not subject to a statutory disqualification as defined in Section 3(a)(39) of the Exchange Act.[176] Proposed paragraph (a)(3)(i)(C) would require that the foreign broker-dealer have in its files information specified in Rule 17a–3(a)(12) under the Exchange Act, including information related to sanctions imposed by foreign securities authorities, foreign exchanges, or foreign associations.[177] Thus, each requires a collection of information by the foreign broker-dealer.

Proposed paragraph (a)(3)(iii)(C) would require that a U.S. registered broker-dealer obtain a representation from the foreign broker-dealer that the foreign broker-dealer has made the determinations that would be required by proposed paragraph (a)(3)(i)(B) and has in its files the information that would be required by proposed paragraph (a)(3)(i)(C). Proposed paragraph (a)(3)(iii)(C) therefore would require a collection of information by both the foreign broker-dealer and the U.S. registered broker-dealer in that the foreign broker-dealer must provide the representation and the U.S. registered broker-dealer must obtain that representation.

Proposed paragraph (a)(3)(iii)(D) would require a U.S. registered broker-dealer to maintain a record of the representations it obtains pursuant to proposed paragraph (a)(3)(iii)(C). This proposed paragraph would require a collection of information by the U.S. registered broker-dealer.

b. Proposed Use of Information

The collections of information under proposed paragraphs (a)(3)(i)(B) and (C) and proposed paragraphs (a)(3)(iii)(C) and (D) are intended to protect U.S. investors from contacts with foreign associated persons with a disciplinary history.

c. Respondents

As discussed above, proposed paragraphs (a)(3)(i)(B) and (C) and proposed paragraphs (a)(3)(iii)(C) and (D) of Rule 15a–6 would require collections of information by both foreign broker-dealers and U.S. registered broker-dealers. All foreign broker-dealers that take advantage of the exemption from registration under the proposed rule would be required to comply with proposed paragraphs (a)(3)(i)(B) and (C) and proposed paragraph (a)(3)(iii)(C). The Commission estimates that approximately 700 foreign broker-dealers would take advantage of the exemption from registration under the proposed rule and therefore be subject to the collection of information requirements in proposed paragraphs (a)(3)(i)(B) and (C) and proposed paragraph (a)(3)(iii)(C).[178]

Similarly, all U.S. registered broker-dealers engaged by foreign broker-dealers to assume the responsibilities of a U.S. registered broker-dealer under the proposed rule, under either exemption, would be required to comply with proposed paragraphs (a)(3)(iii)(C) and (D). The Commission estimates that approximately 40 U.S. registered broker-dealers would be engaged by foreign broker-dealers to assume the responsibilities under Exemption (A)(*1*) and approximately 18 U.S. registered broker-dealers would be engaged by foreign broker-dealers to assume the responsibilities under Exemption (A)(*2*) under the proposed rule, for a total of approximately 58 U.S. registered broker-dealers assuming the responsibilities under paragraph (a)(3)(iii) and therefore be subject to the collection of information requirements in proposed paragraphs (a)(3)(iii)(C) and (D).

d. Reporting and Recordkeeping Burden

The Commission estimates for the purposes of proposed paragraph (a)(3)(i)(B) that each of the approximately 700 foreign broker-dealer respondents would employ approximately 5 foreign associated persons that would effect transactions with qualified investors and would spend approximately 10 hours per year determining that these foreign associated persons are not subject to a statutory disqualification as defined in Section 3(a)(39) of the Exchange Act.[179] The Commission also estimates for the purposes of proposed paragraph (a)(3)(i)(C) that each of the

[172] *See* Part III.D.3., *supra*; *see also* proposed Rule 15a–6(a)(3)(i)(B).

[173] *See* proposed Rule 15a–6(a)(3)(i)(B).

[174] *See* Part III.D.3., *supra*.

[175] *See* 17 CFR 240.15a–6(a)(3)(iii)(C).

[176] *See* proposed Rule 15a–6(a)(i)(B).

[177] *See* proposed Rule 15a–6(a)(i)(C).

[178] Based on information the staff obtained in discussions with industry representatives, the Commission estimates that approximately 40 U.S. registered broker-dealers would serve as U.S. registered broker-dealers under Exemption (A)(*1*) under the proposed rule. The Commission estimates that each of these 40 U.S. registered broker-dealers would do so for an average of 10 foreign broker-dealers, so that an estimated total of 400 foreign broker-dealers would utilize Exemption (A)(*1*) under the proposed rule. The Commission also estimates based on information the staff obtained in discussions with industry that approximately 18 U.S. registered broker-dealers would be engaged under Exemption (A)(*2*) by foreign broker-dealers relying on the exemption provided by paragraph (a)(3)(iii)(A)(*2*) of the proposed rule. The Commission believes that Exemption (A)(*2*) under the proposed rule would be utilized by approximately 300 foreign broker-dealers (an average of 16.67 per each of the 18 U.S. registered broker-dealers acting under Exemption (A)(*2*)—assuming an even distribution of foreign broker-dealers per U.S. registered broker-dealer operating under the exemption, some U.S. registered broker-dealers would do so for 16 foreign broker-dealers and some would do so for 17 foreign broker-dealers). Therefore, the Commission estimates that a total of 700 foreign broker-dealers would take advantage of one or both exemptions from registration under the proposed rule.

[179] As noted above, the bases for these estimates come from information the staff obtained in discussions with industry representatives. Unless otherwise indicated, each of the Commission's estimates used for the purposes of calculating the number of respondents or the burden imposed upon those respondents is based on such discussions.

approximately 700 foreign broker-dealer respondents would spend approximately 10 hours per year complying with the terms of that proposed paragraph. Thus, the Commission estimates for the purposes of proposed paragraph (a)(3)(iii)(C) that each of the approximately 700 foreign broker-dealer respondents would spend approximately 5 hours per year providing representations to U.S. registered broker-dealers that they have complied with proposed paragraphs (a)(3)(i)(B) and (C). Therefore, the annual burden imposed by proposed paragraphs (a)(3)(i)(B) and (C) and proposed paragraph (a)(3)(iii)(C) on each of the 700 foreign broker-dealers would be approximately 25 hours for an aggregate annual burden on all foreign broker-dealers of 17,650 hours (700 foreign broker-dealers × 25 hours per foreign broker-dealer).

The Commission estimates for the purposes of proposed paragraphs (a)(3)(iii)(C) and (D) that each U.S. registered broker-dealer acting under Exemption (A)(*1*) would spend approximately 5 hours each year obtaining and recording representations required by proposed paragraphs (a)(3)(iii)(C) and (D). Similarly, the Commission estimates that each U.S. registered broker-dealer acting under Exemption (A)(*2*) would spend approximately 8 hours each year obtaining and recording representations required by proposed paragraphs (a)(3)(iii)(C) and (D). Thus, the aggregate annual burden imposed by proposed paragraphs (a)(3)(i)(C) and (D) on all U.S. registered broker-dealers would be approximately 344 hours (40 U.S. registered broker-dealers acting under Exemption (A)(*1*) multiplied by 5 hours per broker-dealer plus 18 U.S. registered broker-dealers acting under Exemption (A)(*2*) multiplied by 8 hours per broker-dealer).

e. Collection of Information Is Mandatory

These collections of information would be mandatory for foreign broker-dealers that choose to rely on the exemptions in paragraph (a)(3) of the proposed rule and U.S. registered broker-dealers that intermediate transactions for foreign broker-dealers that choose to rely on the exemptions in paragraph (a)(3) of the proposed rule.

f. Confidentiality

Proposed paragraph (a)(3)(i)(C) would require foreign broker-dealers to have in their files the type of information specified in Rule 17a–3(a)(12) under the Exchange Act, provided that the information required by paragraph (a)(12)(i)(D) of Rule 17a–3 shall include information relating to sanctions imposed by foreign securities authorities, foreign exchanges or foreign associations, including without limitation those described in Section 3(a)(39) of the Exchange Act. Proposed paragraph (a)(3)(iii)(D) would require U.S. registered broker-dealers to maintain a written record of the representations obtained from foreign broker-dealers, as required by proposed paragraph (a)(3)(iii)(C).

All information related to transactions with qualified investors, whether kept by U.S. registered broker-dealers or foreign broker-dealers, would be subject to review and inspection by the Commission and its representatives as required in connection with examinations, investigations and enforcement proceedings. Such information is not required to be disclosed to the public and will be kept confidential by the Commission.

g. Record Retention Period

Proposed paragraphs (a)(3)(i)(B) and (C) and proposed paragraphs (a)(3)(iii)(C) and (D) would not include record retention periods. However, the U.S. registered broker-dealers would have to retain the representations for the period specified under 17 CFR 240.17a–4(b)(7), which requires broker-dealers to preserve all written agreements they enter into relating to their business for a period of not less than three years, the first two years in an easily accessible place.

2. Collection of Information Under Proposed Paragraph (a)(3)(i)(D)

a. Collection of Information

Proposed paragraph (a)(3)(i)(D) would require ''collections of information,'' as that term is defined in 44 U.S.C. 3502(3), by foreign broker-dealers. Proposed paragraph (a)(3)(i)(D) would require that a foreign broker-dealer relying on either Exemption (A)(*1*) or Exemption (A)(*2*) disclose to qualified investors that the foreign broker dealer is regulated by a foreign securities authority and not by the Commission. Foreign broker-dealers relying on Exemption (A)(*1*) would also have to disclose to qualified investors whether U.S. segregation requirements, U.S. bankruptcy protections and protections under the SIPA would apply to any funds and securities held by the foreign broker-dealer.

b. Proposed Use of Information

The collections of information required by proposed paragraph (a)(3)(i)(D) are designed to put U.S. investors on notice that foreign broker-dealers operating pursuant to the exemption in Rule 15a–6(a)(3)(iii)(A)(*1*) are not subject to the same regulatory requirements as U.S. registered broker-dealers. This notice is important because the proposed rule would eliminate the current chaperoning requirements, as described below, and allow a foreign broker-dealer to effect transactions on behalf of qualified investors and custody qualified investor funds and securities relating to any resulting transactions with more limited participation in the transaction by a U.S. registered broker-dealer.[180]

c. Respondents

As discussed above, the Commission estimates that approximately 400 foreign broker-dealers would rely on Exemption (A)(*1*) of the proposed rule. All 400 foreign broker-dealers would be required to comply with proposed paragraph (a)(3)(i)(D). The Commission also estimates that approximately 300 foreign broker-dealers would rely on Exemption (A)(2) of the proposed rule. These 300 foreign broker-dealers would only be required to comply with proposed paragraph (a)(3)(i)(D)(*1*).

d. Reporting and Recordkeeping Burden

Each of the 700 foreign broker-dealers that would rely on either Exemption (A)(*1*) or Exemption (A)(*2*) of the proposed rule would have to make certain disclosures required by proposed paragraph (a)(3)(i)(D) to each qualified investor from which the foreign broker-dealer induces or attempts to induce the purchase or sale of any security. The Commission believes that such disclosures would be conveyed in the course of other communications between the foreign broker-dealer and the qualified investor, such as the foreign broker-dealer's standard account-opening documentation. Thus, we expect that the only collection of information burden that proposed paragraph (a)(3)(i)(D) would impose on a foreign broker-dealer would be the hour burden incurred in developing and updating as necessary the standard documentation it will provide to qualified investors. In addition, the Commission does not believe that there would be a significant difference in the burden placed foreign broker-dealers relying on either Exemption (A)(*1*) or Exemption (A)(*2*) of the proposed rule by proposed paragraph (a)(3)(i)(D). The Commission

[180] Similarly, because of the limited participation of the U.S. registered broker-dealer and the lack of chaperoning requirements, the proposed rule would require that the foreign broker-dealer be regulated for conducting securities activities in a foreign country by a foreign securities authority.

estimates that each of the 700 foreign broker-dealers that would rely on either Exemption (A)(*1*) or Exemption (A)(*2*) of the proposed rule would spend approximately 2 hours per year in drafting, reviewing or updating as necessary their standard documentation for compliance with proposed paragraph (a)(3)(i)(D). Therefore, the aggregate annual collection of information burden imposed by proposed paragraph (a)(3)(i)(D) on foreign broker-dealers would be approximately 1,400 hours (700 foreign broker-dealers multiplied by 2 hours per foreign broker-dealer).

e. Collection of Information Is Mandatory

This collection of information would be mandatory for foreign broker-dealers that rely on either Exemption (A)(*1*) or Exemption (A)(*2*) of the proposed rule.

f. Confidentiality

The disclosures required by proposed paragraph (a)(3)(i)(D) would be conveyed to a qualified investor in the course of communications between the foreign broker-dealer and the qualified investor, such as the foreign broker-dealer's standard account-opening documentation, and therefore would not be confidential.

g. Record Retention Period

Proposed paragraph (a)(3)(i)(D) would not include a record retention period.

3. Related Collections of Information Under Proposed Paragraphs (a)(3)(iii)(B) and (D)

a. Collection of Information

Proposed paragraphs (a)(3)(iii)(B) and (D) would require ''collections of information,'' as that term is defined in 44 U.S.C. 3502(3), by U.S. registered broker-dealers. Proposed paragraph (a)(3)(iii)(B) would require that a U.S. registered broker-dealer obtain from a foreign broker-dealer and each of the foreign broker-dealer's foreign associated persons written consents to service of process for any civil action brought by or proceeding before the Commission or a self-regulatory organization (as defined in Section 3(a)(26) of the Exchange Act).[181] Proposed paragraph (a)(3)(iii)(D) would require that the U.S. registered broker-dealer maintain a written record of the consents to service of process obtained pursuant to proposed paragraph (a)(3)(iii)(B).

b. Proposed Use of Information

The collections of information under proposed paragraphs (a)(3)(iii)(B) and (D) are designed to assist the Commission in its regulatory function by ensuring that foreign broker-dealers and their foreign associated persons effecting transactions with qualified investors have consented to service of process.

c. Respondents

All U.S. registered broker-dealers engaged by foreign broker-dealers to assume the responsibilities of a U.S. registered broker-dealer under the proposed exemption would be subject to the collections of information. As discussed above, the Commission estimates that approximately 40 U.S. registered broker-dealers would act under Exemption (A)(*1*) for foreign broker-dealers relying on the exemption provided by paragraph (a)(3)(iii)(A)(*1*) of the proposed rule and that approximately 18 U.S. registered broker-dealers would act under Exemption (A)(*2*). Therefore, the Commission estimates that a total of approximately 58 U.S. registered broker-dealers would have to comply with the collection of information requirements in proposed paragraphs (a)(3)(iii)(B) and (D).[182]

d. Reporting and Recordkeeping Burden

As discussed above, the Commission estimates that each of the 40 U.S. registered broker-dealers that would serve under Exemption (A)(*1*) for affiliated foreign broker-dealers under the proposed rule would do so for an average of 10 foreign broker-dealers. The Commission also estimates that each such foreign broker-dealer would have an average of 5 foreign associated persons engaged in business under the proposed rule. Therefore, proposed paragraphs (a)(3)(iii)(B) and (D) would require each U.S. registered broker-dealer acting under Exemption (A)(*1*) to obtain and record a total of 50 consents to service of process from foreign associated persons and 10 consents to service of process from foreign broker-dealers.

As discussed above, the Commission estimates that each of the 18 U.S. registered broker-dealers that would serve under Exemption (A)(*2*) for qualified investors would do so for approximately 16.67 foreign broker-dealers. Also as discussed above, the Commission estimates that each such foreign broker-dealer would have an average of 5 foreign associated persons engaged in business under the proposed rule. Therefore, proposed paragraphs (a)(3)(iii)(B) and (D) would require a U.S. registered broker-dealer acting under Exemption (A)(*2*) to obtain a total of 83.35 consents to service of process from foreign associated persons and 16.67 consents to service of process from foreign broker-dealers.[183]

The Commission further estimates that each affected U.S. registered broker-dealer, acting under either exemption, would spend an average of 0.5 hours in obtaining and recording one consent under proposed paragraphs (a)(3)(iii)(B) and (D). Each U.S. registered broker-dealer acting under Exemption (A)(*1*) would therefore spend an average of 35 hours per year in its efforts at compliance with proposed paragraphs (a)(3)(iii)(B) and (D) (0.5 hours per consent per representation multiplied by the sum of 50 consents from foreign associated persons plus 10 consents to service of process from foreign broker-dealers plus 10 representations). Similarly, each U.S. registered broker-dealer acting under Exemption (A)(*2*) would spend an average of 50.01 hours per year in its efforts at compliance with proposed paragraphs (a)(3)(iii)(B) and (D) (0.5 hours per consent per representation multiplied by the sum of 83.35 consents from foreign associated persons plus 16.67 consents to service of process from foreign broker-dealers). Therefore, the Commission estimates an annual aggregate reporting and recordkeeping burden of 2,300.18 hours for compliance with proposed paragraphs (a)(3)(iii)(B) and (D) (35 hours per 40 registered broker-dealers acting under Exemption (A)(*1*) for a total of 1,400 hours, plus 50.01 hours per 18 registered broker-dealers acting under Exemption (A)(*2*) for a total of 900.18 hours).

e. Collection of Information Is Mandatory

This collection of information would be mandatory for U.S. registered broker-dealers that intermediate transactions for foreign broker-dealers that choose to

[181] The consent would indicate that process may be served on the foreign broker-dealer or foreign associated person by service on the U.S. registered broker-dealer in the manner set forth on the U.S. registered broker-dealer's current Form BD. *See* proposed Rule 15a–6(a)(3)(iii)(B).

[182] The Commission understands that U.S. registered broker-dealers acting under Exemption (A)(*2*) are likely to also act under Exemption (A)(*1*) under the proposed rule. The Commission requests comment regarding how frequently this would occur.

[183] Assuming a relatively even distribution of the estimated 300 foreign broker-dealers across the 18 U.S. registered broker-dealers acting under Exemption (A)(*2*), proposed paragraphs (a)(3)(iii)(B) and (D) would require some U.S. registered broker-dealers acting under Exemption (A)(*2*) to obtain and record 83 consents to service of process from foreign associated persons and some to obtain and record 84 consents to service of process from foreign associated persons.

rely on the exemption in paragraph (a)(3) of the proposed rule.

f. Confidentiality

The proposed rule would require that U.S. registered broker-dealers maintain a written record of the information and consents and make such records available to the Commission upon request. All information related to transactions with qualified investors, whether kept by U.S. registered broker-dealers or foreign broker-dealers, would be subject to review and inspection by the Commission and its representatives as required in connection with examinations, investigations and enforcement proceedings. Such information is not required to be disclosed to the public and will be kept confidential by the Commission.

g. Record Retention Period

Proposed paragraphs (a)(3)(iii)(B) and (D) would not include separate record retention periods. However, the U.S. registered broker-dealers would have to retain the consents for the period specified under 17 CFR 240.17a–4(b)(7), which requires broker-dealers to preserve all written agreements they enter into relating to their business for a period of not less than three years, the first two years in an easily accessible place.

4. Related Collections of Information Under Proposed Paragraph (a)(4)(vi)(B)

Under the proposed rule, a foreign broker-dealer would be exempt from the registration, reporting and other requirements of the Exchange Act to the extent that it effects transactions in securities with or for, or induces or attempts to induce the purchase or sale of any security by any U.S. person, other than a registered broker-dealer or bank acting pursuant to an exception or exemption from the definition of ''broker'' or ''dealer'' in Section 3(a)(4)(B), 3(a)(4)(E), or 3(a)(5)(C) of the Exchange Act or the rules thereunder, that acts in a fiduciary capacity for an account of a foreign resident client.[184] As a condition of this exemption, the foreign broker-dealer would be required, among other things, to obtain and maintain a representation from the U.S. person that the account is managed in a fiduciary capacity for a foreign resident client.[185]

a. Collection of Information

Proposed paragraph (a)(4)(vi)(B) would require ''collections of information'' as that term is defined in 44 U.S.C. 3502(3) in that it would require foreign broker-dealers to obtain and maintain a representation for each account managed by a U.S. fiduciary that the account is managed in a fiduciary capacity for a foreign resident client. This would require foreign broker-dealers to obtain and record each representation. The proposed paragraph would also require a collection of information by the U.S. fiduciary, which would be required to provide the representation to the foreign broker-dealer.

b. Proposed Use of Information

The collection of information in proposed paragraph (a)(4)(vi)(B) would assist foreign broker-dealers seeking to rely on the exemption under proposed paragraph (a)(4)(vi) in complying with the terms of that exemption and would provide the Commission with access to such information.

c. Respondents

As discussed above, the Commission estimates that approximately 700 foreign broker-dealers that would take advantage of either exemption under proposed paragraphs (a)(3)(iii)(A)(*1*) and (*2*).[186] The Commission believes that these estimated 700 foreign broker-dealers represent the number of foreign broker-dealers that engage in international broker-dealer business and would take advantage of the exemption in proposed paragraph (a)(4)(vi). Even though not all of these 700 foreign broker-dealers may actually utilize the exemption in proposed paragraph (a)(4)(vi), for the purposes of determining the number of foreign broker-dealer respondents for the collection of information in proposed paragraph (a)(4)(vi)(B), the Commission estimates that all 700 foreign broker-dealers that engage in international business and that would otherwise take advantage of either exemption under proposed paragraph (a)(3)(iii)(A)(*1*) or (*2*) would also utilize the exemption in proposed paragraph (a)(4)(vi) and be respondents for the purposes of the collection of information in proposed paragraph (a)(4)(vi)(B).

The Commission estimates that there are 349 U.S. fiduciaries that would be respondents for the purposes of the collection of information in proposed paragraph (a)(4)(vi)(B).

d. Reporting and Recordkeeping Burden

The Commission estimates that each U.S. fiduciary would spend approximately 5 hours per year providing representations in accordance with proposed paragraph (a)(4)(vi)(B). Therefore, the Commission estimates that the aggregate burden imposed by proposed paragraph (a)(4)(vi)(B) on all of the approximately 349 U.S. fiduciaries would be approximately 1,745 hours per year (5 hours multiplied by 349 U.S. fiduciaries).

The Commission also estimates that each foreign broker-dealer would spend approximately 5 hours per year obtaining and recording the representations required by proposed paragraph (a)(4)(vi)(B) from U.S. fiduciaries. Therefore, the Commission estimates that the aggregate burden imposed by proposed paragraph (a)(4)(vi)(B) on all the approximately 700 foreign broker-dealers would be approximately 3,500 hours per year (5 hours multiplied by 700 foreign broker-dealers).

e. Collection of Information Is Mandatory

These collections of information would be mandatory for U.S. fiduciaries and foreign broker-dealers that effect transactions according to the proposed exemption in proposed paragraph (a)(4)(vi) of the proposed rule.

f. Confidentiality

The proposed rule would require that a foreign broker-dealer maintain the representations it would obtain from a U.S. fiduciary regarding the U.S. fiduciary's accounts. All information related to transactions with qualified investors, whether kept by U.S. registered broker-dealers or foreign broker-dealers, would be subject to review and inspection by the Commission and its representatives as required in connection with examinations, investigations and enforcement proceedings. Such information is not required to be disclosed to the public and will be kept confidential by the Commission.

g. Record Retention Period

Proposed paragraph (a)(4)(vi)(B) would not include a record retention period.

5. Request for Comment

The Commission requests comment on the proposed collections of information in order to: (1) Evaluate whether the proposed collection of information is necessary for the proper performance of the functions of the Commission, including whether the information would have practical utility; (2) evaluate the accuracy of the Commission's estimates of the burden of the proposed collections of information; (3) determine whether there are ways to

[184] *See* proposed paragraph (a)(4)(vi).

[185] *See* proposed paragraph (a)(4)(vi)(B).

[186] *See* note 178, *supra*.

enhance the quality, utility and clarity of the information to be collected; (4) evaluate whether there are ways to minimize the burden of the collection of information on those who respond, including through the use of automated collection techniques or other forms of information technology; and (5) evaluate whether the proposed rules would have any effects on any other collection of information not previously identified in this section.

Persons who desire to submit comments on the collection of information requirements should direct their comments to OMB, Attention: Desk Officer for the Securities and Exchange Commission, Office of Information and Regulatory Affairs, Washington, DC 20503, and should also send a copy of their comments to Secretary, Securities and Exchange Commission, 100 F Street, NE., Washington, DC 20549–1090, and refer to File No. S7–16–08. OMB is required to make a decision concerning the collections of information between 30 and 60 days after publication of this document in the **Federal Register**; therefore, comments to OMB are best assured of having full effect if OMB receives them within 30 days of this publication. Requests for the materials submitted to OMB by the Commission with regard to these collections of information should be in writing, refer to File No. S7–16–08, and be submitted to the Securities and Exchange Commission, Records Management Office, 100 F Street, NE, Washington, DC 20549–1110.

B. Consideration of Benefits and Costs

1. Expected Benefits

The proposed rule would have several important benefits. First, the proposed rule would allow a broader category of U.S. investors [187] greater access to foreign broker-dealers and foreign markets by expanding and streamlining the conditions under which a foreign broker-dealer could operate without triggering the registration requirements of Section 15(a)(1) or 15B(a)(1) of the Exchange Act. Among the benefits to U.S. investors would be expanded investment and diversification opportunities and lower cost of accessing such opportunities. Because the proposed rule would broaden the category of U.S. investors that may interact with foreign broker-dealers, the expanded investment and diversification opportunities would be available to a greater number of U.S. investors that the Commission believes possess the investment experience to effect transactions with or through unregistered broker-dealers under the safeguards imposed by the proposed rule. This also would be a benefit to foreign broker-dealers, which would have access to an expanded potential client base without being required to register with the Commission as broker-dealers.

In addition, the Commission understands that the current chaperoning requirements have been criticized as impractical and imposing unnecessary operational and compliance burdens, particularly for communications with broker-dealers in time zones outside those of the United States. In this regard, the Commission believes that the investor protections intended to be provided by the presence of associated persons of U.S. registered broker-dealers during in-person or telephonic communications between foreign associated persons of foreign broker-dealers and U.S. investors, as under the current rule, could be achieved by less operationally challenging methods. Specifically, foreign associated persons that are subject to statutory disqualification specified in Section 3(a)(39) of the Exchange Act would be precluded from contacting qualified investors and foreign broker dealers would be required to make disclosures to those investors, placing them on notice that the foreign broker-dealer is regulated by a foreign securities authority and not by the Commission and, in the case of Exemption (A)(*1*), informing them that U.S. segregation requirements, U.S. bankruptcy protections and protections under the SIPA would apply to any funds and securities held by the foreign broker-dealer.[188] Accordingly, the proposed rule would allow a foreign broker-dealer to have unchaperoned visits within the United States and communications, both oral and electronic, with qualified investors, as long as a U.S. registered broker-dealer assumes certain limited responsibilities in connection with the foreign broker-dealer's activities, as described above. As a result, the proposed rule should facilitate communications between foreign broker-dealers and qualified investors to communicate, while utilizing more efficient methods designed to protect qualified investors.

Second, the proposed rule would provide U.S. registered broker-dealers and foreign broker-dealers with greater flexibility in how they conduct business under paragraph (a)(3) of Rule 15a–6. For instance, U.S. registered broker-dealers acting under Exemption (A)(*1*) would be allowed to maintain copies of books and records in the form prescribed by the foreign securities authority and with the foreign broker-dealer. In general, the proposed rule would allow a foreign broker-dealer to effect transactions on behalf of qualified investors and custody qualified investor funds and securities relating to any resulting transactions with more limited participation in the transaction by a U.S. registered broker-dealer. Among other things, this would have the benefit of eliminating the need for the U.S. registered broker-dealer to ''double book'' transactions under current Rule 15a–6(a)(3). It would also allow the foreign broker-dealer more flexibility in how it communicates with qualified investors, as described above.

Third, while proposed Rule 15a–6 would impose certain costs on U.S. registered broker-dealers acting under either exemption, as discussed below, these costs would be markedly less than under current Rule 15a–6. Most importantly, the proposed rule would significantly reduce the cost for a U.S. registered broker-dealer to intermediate transactions under paragraph (a)(3) of Rule 15a–6.

Under Exemption (A)(*1*), the U.S. registered broker-dealer would not be required to effect transactions—and perform all of the functions associated with effecting transactions, including, for example, compliance with recording and recordkeeping rules, issuing confirmations and maintaining custody of customer funds and securities—on behalf of the qualified investor. Instead, under the proposed rule, the U.S. registered broker-dealer would only be required to collect and make available to the Commission certain limited information. Specifically, the proposed rule would require a U.S. registered broker-dealer acting under Exemption (A)(*1*) to maintain certain books and records, including confirmations and statements issued by the foreign broker-dealer to the qualified investor, but would permit the U.S. registered broker-dealer to maintain those books and records in the form, manner and for the

[187] As noted above, the proposed rule would expand the category of U.S. investors with which a foreign broker-dealer may interact under Rule 15a–6(a)(2) from major U.S. institutional investors to qualified investors and generally expand the category of U.S. investors with which a foreign broker-dealer may interact under Rule 15a–6(a)(3) from major U.S. institutional investors and U.S. institutional investors to qualified investors. This would allow foreign broker-dealers, for the first time, to interact with a corporation, company, or partnership that owns and invests on a discretionary basis $25 million or more in investments under paragraph (a)(3). In addition, under the proposed rule, natural persons who own or invest on a discretionary basis not less than $25,000,000 in investments would be included. *See* Part III.A., *supra*.

[188] *See* proposed Rule 15a–6(a)(3)(i)(B) and (D).

periods prescribed by the foreign securities authority regulating the foreign broker-dealer and with the foreign broker-dealer.[189] The Commission believes that all U.S. registered broker-dealers acting under Exemption (A)(*1*) in Rule 15a–6(a)(3) relationships would take advantage of this option, thereby significantly lowering costs associated with collecting and maintaining books and records, including collection of information burdens under the Paperwork Reduction Act and associated costs. There would also be significant cost savings for U.S. registered broker-dealers acting under Exemption (A)(*1*) because they would not have to clear and settle transactions, safeguard customer funds and securities, or issue confirmations.

In addition, regardless of whether the U.S. registered broker-dealer acts under Exemption (A)(*1*) or Exemption (A)(*2*), the proposed rule would eliminate the current rule's requirement that the U.S. registered broker-dealer make certain determinations regarding the foreign broker-dealer and its associated persons. Under the proposed rule, the U.S. registered broker-dealer would only be required to obtain representations from the foreign broker-dealer regarding that information.[190] This would be a significant cost savings with respect to the current rule because the U.S. registered broker-dealer would not have to make the determination itself for each foreign broker-dealer and its associated persons as under the current rule.

Finally, the proposed rule would reduce a foreign broker-dealer's costs of meeting the conditions of the exemption in two principal ways. First, the proposed amendments would make it less burdensome for foreign broker-dealers to communicate directly with qualified investors. Currently, Rule 15a–6 requires an associated person of a U.S. registered broker-dealer to chaperone certain in-person visits and oral communications between foreign associated persons and U.S. institutional investors, with certain exceptions, and chaperone in-person visits between foreign associated persons and major U.S. institutional investors under certain conditions.[191] The proposed rule would allow a foreign broker-dealer to hold in-person meetings and have oral and electronic communications with qualified investors without the intermediation of an U.S. registered broker-dealer. This would result in significant cost savings.

Second, the proposed rule would provide a foreign broker-dealer with the alternative of having a U.S. registered broker-dealer act under Exemption (A)(*1*) or under Exemption (A)(*2*). These alternatives would allow the foreign broker-dealer and the U.S. registered broker-dealer, as well as the qualified investors, to determine the most cost effective method for complying with the rule.

2. Expected Costs

Of course, reducing the cost of complying with paragraph (a)(3) of Rule 15a–6 may encourage more U.S. registered broker-dealers and foreign broker-dealers to rely on the rule, which would increase the overall costs associated with complying with the requirements of Rule 15a–6. As noted above, the increased flexibility of the proposed rule would provide U.S. investors with increased access to foreign broker-dealers and foreign markets, which would presumably lead to increased transactional activity under Rule 15a–6(a)(3). As a result, foreign broker-dealers may experience some incremental cost increase. In addition, because some of the responsibilities under paragraph (a)(3) of the proposed rule would be shifted to the foreign broker-dealer, foreign broker-dealers may incur some greater costs, some of which are described below. We believe these increased costs would be insignificant. For example, because foreign broker-dealers, as members of foreign exchanges, typically are required to clear and settle transactions in foreign securities, regardless of the requirements of Rule 15a–6(a)(3), shifting the responsibility for clearing and settling from the U.S. registered broker-dealer to foreign broker-dealers would not increase their cost of complying with Rule 15a–6. Similarly, other foreign governments or securities regulators may have laws or rules comparable to the provisions in Section 3(a)(39) of the Exchange Act related to statutory disqualification. Requiring foreign broker-dealers to review the fitness of their associated persons under the provisions of Section 3(a)(39), in addition to meeting the requirements of equivalent foreign laws or rules, would impose an incremental cost on those foreign broker-dealers.

Shifting some of the responsibilities under paragraph (a)(3) of the proposed rule to foreign broker-dealers would have an effect on the business activities of U.S. registered broker-dealers. For example, shifting the responsibility for clearing and settling from the U.S. registered broker-dealer to foreign broker-dealers would reduce the compensation received by U.S. registered broker-dealers for these and other services. The elimination of the chaperoning requirements of the current rule may also reduce income to U.S. registered broker-dealers that perform such services for foreign broker-dealers.

In addition, as described above, certain provisions of the proposed rule would impose ''collection of information'' requirements within the meaning of the Paperwork Reduction Act on foreign broker-dealers, U.S. registered broker-dealers and U.S. fiduciaries.[192] For each of the collections of information that would be imposed by the proposed rule, the relevant respondent or respondents would incur an hour burden in complying with the collection of information requirements. For example, as described above, proposed paragraph (a)(3)(i)(B) would require that a foreign broker-dealer make a determination that its foreign associated persons effecting transactions with a qualified investor are not subject to a statutory disqualification. As explained, we estimate each foreign broker-dealer that takes advantage of the exemption under the proposed rule would spend approximately 10 hours per year in making the determination required by proposed paragraph (a)(3)(i)(B). While not a burden for the purposes of the PRA, the foreign broker-dealer would also incur certain costs related to the 10 hours per year spent making the determination required by proposed paragraph (a)(3)(i)(B). Specifically, the determination likely would be made by an employee of the foreign broker-dealer to whom the broker-dealer must pay a salary or hourly wage. Therefore, the salaries and wages foreign broker-dealers, U.S. registered broker-dealers and U.S. fiduciaries must pay to the employees who would perform the work required by the collections of information imposed by the proposed rule would be additional costs of meeting the exemption in the proposed rule. These costs are described in the following paragraphs.

a. Collection of Information Costs to Foreign Broker-Dealers

As described above in the Paperwork Reduction Act Analysis, proposed paragraphs (a)(3)(i)(B), (a)(3)(i)(C), (a)(3)(i)(D), (a)(3)(iii)(C) and (a)(4)(vi)(B) each would impose collection of

[189] *See* proposed Rule 15a–6(a)(3)(iii)(A)(*1*) and (*2*).

[190] *See* proposed Rule 15a–6(a)(3)(iii)(C).

[191] *See* 17 CFR 240.15a–6(a)(3)(ii)(A)(*1*) and (iii)(B). This would be a cost savings for U.S. registered broker-dealers as well, as they would no longer need to chaperone the in-person visits and oral communications of foreign associated persons with U.S. investors.

[192] *See* Part VI.A., *supra*.

information requirements on foreign broker-dealers. Other than proposed paragraph (a)(3)(i)(C), these collections of information would require the foreign broker-dealer to make certain legal determinations, provide or obtain legal representations or draft disclosures. Therefore, the Commission believes that the type of work required by each requirement would be performed by a compliance attorney at each foreign broker-dealer. Proposed paragraph (a)(3)(i)(C), however, is a record-keeping requirement and the Commission believes that this type of work would be performed by a compliance clerk at each foreign broker-dealer.

The Commission estimates that foreign broker-dealers pay compliance attorneys at an hourly rate of (U.S.) $270.00 and compliance clerks at an hourly rate of (U.S.) $62.00.[193] Based on the estimates of the hourly burden imposed by proposed paragraphs (a)(3)(i)(B), (a)(3)(i)(B), (a)(3)(i)(D), (a)(3)(iii)(C) and (a)(4)(vi)(B) on foreign broker-dealers, the Commission further estimates that foreign broker-dealers would incur a total cost of (U.S.) $6,560.00 per year complying with the collection of information requirements that would be imposed by those paragraphs.[194]

b. Collection of Information Costs to U.S. Registered Broker-Dealers

As described above in the Paperwork Reduction Act Analysis, proposed paragraphs (a)(3)(iii)(B), (C) and (D) each would impose collection of information requirements on U.S. registered broker-dealers. These collections of information would require the U.S. registered broker-dealer to obtain and record certain legal representations made by foreign broker-dealers. The Commission believes that this type of work would be performed by a compliance attorney at each U.S. registered broker-dealer. The Commission estimates that U.S. registered broker-dealers pay compliance attorneys at an hourly rate of (U.S.) $270.00. Based on the estimates of the hourly burden imposed by proposed paragraphs (a)(3)(iii)(B), (C) and (D) on U.S. registered broker-dealers, the Commission further estimates that U.S. registered broker-dealers intermediating transactions for foreign broker-dealers relying on Exemption (A)(*1*) would incur a total cost of (U.S.) $10,800.00 per year complying with the collection of information requirements that would be imposed by those paragraphs.[195] The Commission estimates that U.S. registered broker-dealers intermediating transactions for foreign broker-dealers relying on Exemption (A)(*2*) would incur a total cost of (U.S.) $13,527.00 per year complying with the collection of information requirements that would be imposed by those paragraphs.[196]

c. Collection of Information Costs to U.S. Fiduciaries

As described above in the Paperwork Reduction Act Analysis, proposed paragraph (a)(4)(vi)(B) would impose collection of information requirements on U.S. fiduciaries in the form of a legal representation provided to foreign broker-dealers that, for each account managed by a U.S. fiduciary, the account is managed in a fiduciary capacity for a foreign resident client. The Commission believes that these legal representations would be made by a compliance attorney at each U.S. fiduciary.

The Commission estimates that U.S. fiduciaries pay compliance attorneys at an hourly rate of (U.S.) $270.00. Based on the estimates of the hourly burden imposed by proposed paragraphs (a)(4)(vi)(B) on U.S. fiduciaries, the Commission further estimates that U.S. fiduciaries would incur a total cost of (U.S.) $1,350.00 per year complying with the collection of information requirements that would be imposed by that paragraph (5 hours per year at $270.00 per hour = $1,350.00 per year).[197]

3. Comment Solicited

We solicit comment on the costs and benefits to U.S. investors, foreign broker-dealers, U.S. registered broker-dealers and others who may be affected by the proposed amendments to Rule 15a–6. We request views on the costs and benefits described above as well as on any other costs and benefits that could result from adoption of the proposed rule amendments. The Commission renews its request for comment on the Commission's estimates of the hour burdens that would be imposed by the collections of information in the proposed rule and also solicits comment on its calculation of the monetary cost of those burdens. In particular, the Commission requests comment on whether the work required by the collections of information would be performed by the individuals identified. For the cost of work that would be performed by employees of foreign broker-dealers, is it reasonable to assume that such employees generally earn salaries and wages similar to comparable employees of U.S. registered broker-dealers, after conversion to U.S. dollars? Commenters are requested to provide empirical data and other factual support for their views, if possible.

C. Consideration of Burden on Competition, and on Promotion of Efficiency, Competition and Capital Formation

Section 3(f) of the Exchange Act 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 whether the action would promote efficiency, competition and capital formation.[198] Exchange Act Section 23(a)(2) requires the Commission, in making rules under the Exchange Act, to consider the impact that any such rule would have on competition. This section 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.[199]

The Commission believes the proposed amendments would not impose any burden on competition not necessary or appropriate in furtherance of the Exchange Act. By streamlining the conditions under which a foreign broker-dealer may operate without

[193] *See* Securities Industry and Financial Markets Association's ''Management & Professional Earnings in the Securities Industry—2007'' (available at: *http://www.sifma.org/research/surveys/professional-earning.shtml*). The SIFMA study reflects a survey of U.S. earnings. We estimate that the earnings of comparable employees at foreign broker-dealers are similar, but solicit comment on whether foreign salaries vary and, if so, how.

[194] 10 hours per year at $270.00 per hour complying with proposed paragraph (a)(3)(i)(B), 10 hours per year at $62.00 per hour complying with proposed paragraph (a)(3)(i)(C), 2 hours per year at $270.00 per hour complying with proposed paragraph (a)(3)(i)(D), 5 hours per year at $270.00 per hour complying with proposed paragraph (a)(3)(iii)(C) and 5 hours per year at $270.00 per hour complying with proposed paragraph (a)(4)(vi)(B). *See* Part VI.A., *supra*.

[195] 5 hours per year at $270.00 per hour and 35 hours per year at $270.00 per hour. *See id.*

[196] 8 hours per year at $270.00 per hour and 50.1 hours per year at $270.00 per hour. *See id.* As discussed above in the PRA analysis, U.S. registered broker-dealers intermediating transactions for foreign broker-dealers relying on Exemption (A)(*1*) would spend different amounts of time complying with the collection of information requirements of proposed paragraphs (a)(3)(iii)(B), (C) and (D) than U.S. registered broker-dealers intermediating transactions for foreign broker-dealers relying on Exemption (A)(*2*). *See* Part VI.A., *supra*. Therefore, the monetary costs incurred in complying with these paragraphs would also be different for intermediating U.S. registered broker-dealers, depending on the exemption relied upon by the foreign broker-dealer. *See id.*

[197] *See id.*

[198] 15 U.S.C. 78c(f).

[199] 15 U.S.C. 78w(a)(2).

triggering the registration requirements of Section 15(a)(1) or 15B(a)(1) of the Exchange Act and the reporting and other requirements of the Exchange Act (other than Sections 15(b)(4) and 15(b)(6)), the proposed amendments to Rule 15a–6 should promote competition by enhancing the ability of foreign broker-dealers to compete with U.S. registered broker-dealers in the U.S. market, particularly with respect to transactions in foreign securities.[200]

We note, in particular, that making Exemption (A)(1) available only to a foreign broker-dealer conducting a predominantly foreign business would provide U.S. investors increased access to foreign expertise and foreign securities and markets without creating opportunities for regulatory arbitrage vis-à-vis U.S. securities markets.[201] As discussed above, this is particularly important because, under Exemption (A)(1), for the first time, a foreign broker-dealer would be able to provide full-service brokerage services (including maintaining custody of funds and securities from resulting transactions) to U.S. investors.[202] We are proposing an 85 percent threshold for determining whether a foreign broker-dealer conducts a predominantly foreign business because a lower threshold may allow a foreign broker-dealer to conduct significant business in U.S. securities with U.S. investors without being regulated by the Commission. While we believe that the 85% threshold would be effective in eliminating the opportunities for regulatory arbitrage, allowing foreign broker-dealers to conduct any business in U.S. securities could affect the competitive positions of U.S. registered broker-dealers and foreign broker-dealers.[203]

Exemption (A)(*2*), which would not require a foreign broker-dealer to conduct a predominantly foreign business, would allow foreign broker-dealers to compete more directly with U.S. registered broker-dealers without limitation on the type of security, U.S. or foreign. In order to preserve measures of investor protection, however, the proposed rule would require a U.S. registered broker-dealer to keep books and records and act as custodian of funds and securities.[204]

We solicit comment on whether the proposed amendments would promote competition, including whether investors would be more or less likely to choose to invest in foreign markets under the proposed rule.

The Commission also believes the proposed amendments would promote efficiency. As U.S. investors increasingly invest in securities whose primary market is outside the United States, the ability of these investors to obtain ready access to foreign markets has grown in importance.[205] In some cases, foreign broker-dealers may offer such access to these U.S. investors by more efficient means than a U.S. registered broker-dealer could. For example, a foreign broker-dealer may more efficiently provide a U.S. investor with the means to execute trades quickly in a wide range of foreign securities markets. A foreign broker-dealer may also offer expertise and access to research reports concerning foreign companies, industries and market environments.[206] Allowing foreign broker-dealers to provide these services to certain classes of U.S. investors without registering, but subject to the conditions of proposed Rule 15a–6, would further stimulate the competition and efficiencies promoted by the current rule.

The proposed amendments to Rule 15a–6 are intended to promote efficiency by reducing the costs of compliance for both U.S. registered broker-dealers and foreign broker-dealers conducting transactions pursuant to paragraph (a)(3). As discussed above, the proposed rule should decrease the burden on U.S. registered broker-dealers acting under both Exemption (A)(*1*) and Exemption (A)(*2*) for foreign broker-dealers. While some of this burden would be shifted to foreign broker-dealers, overall the burden of complying with the proposed rule would be lessened. As a result, we believe that the proposed rule would enable U.S. investors to more efficiently gain access to foreign broker-dealers.

Although the proposed amendments may facilitate capital formation and capital raising by foreign broker-dealers by increasing the available pool of U.S. investors foreign broker-dealers can contact directly, the Commission does not believe that they would have any significant effect on capital formation. We note that U.S. investors can currently obtain access to foreign securities through U.S. broker-dealers.

We solicit comment on whether the proposed amendments would impose a burden on competition or whether they would promote efficiency, competition and capital formation. Commenters are requested to provide empirical data and other factual support for their views if possible.

D. Consideration of the Impact on the Economy

For purposes of the Small Business Regulatory Enforcement Fairness Act of 1996, or ''SBREFA,''[207] the Commission must advise the Office of Management and Budget as to whether the proposed amendments to Rule 15a–6 constitute a ''major'' rule. Under SBREFA, a rule is considered ''major'' where, if adopted, it would result or is likely to result in: An annual effect on the economy of $100 million or more (either in the form of an increase or a decrease); a major increase in costs or prices for consumers or individual industries; or a significant adverse effect on competition, investment, or innovation.

If a rule is ''major,'' its effectiveness would generally be delayed for 60 days pending Congressional review. We request comment on the potential impact of the proposed amendments on the economy on an annual basis. Commenters are requested to provide empirical data and other factual support for their views to the extent possible.

E. Regulatory Flexibility Certification

Section 3(a) of the Regulatory Flexibility Act (''RFA'') requires the Commission to undertake an initial regulatory flexibility analysis of the impact of a proposed rule on small entities, unless the Commission certifies that the rule, if adopted, would not have a significant economic impact on a substantial number of small entities. The application of the RFA to proposed Rule 15a–6 is limited, because its exemptive provisions would be restricted to foreign broker-dealers, which need not be considered under the RFA. In addition, to the extent that the proposed rule, if adopted, would impose any costs on U.S. registered broker-dealer affiliates of such foreign broker-dealers or on other domestic broker-dealers, those costs are not significant and would not impact a substantial number of small domestic broker-dealers. Staff discussions with industry have indicated that small domestic broker-dealers generally are not engaged in Rule 15a–6(a)(3) arrangements with foreign broker-dealers, and have not indicated that this would change in the event the conditions of the rule were amended. Accordingly, the Commission certifies that the proposed rule, if adopted, would not have a significant economic

[200] *See* generally, Part III.D.1., *supra*.

[201] *See* Part III.D.1.a., *supra*.

[202] *See id*.

[203] *See* Part III.D.1.a.ii., *supra*.

[204] *See* Part III.D.1.b.i., *supra*.

[205] *See* Part III.A., *supra*.

[206] *See generally,* Part III.D.1., *supra*.

[207] Pub. L. 104–121, Title II, 110 Stat. 857 (1996) (codified in various sections of 5 U.S.C., 15 U.S.C. and as a note to 5 U.S.C. 601).

impact on a substantial number of small entities.

VII. Statutory Basis

Pursuant to the Exchange Act and particularly sections 3, 10, 15, 17, 23, 30 and 36 thereof, 15 U.S.C. 78c, 78j, 78o, 78q, 78w, 78dd and 78mm, the Commission proposes to amend § 240.15a–6 of Title 17 of the Code of Federal Regulations in the manner set forth below.

VIII. Text of Proposed Amendments

Lists of Subjects in 17 CFR Part 240

Broker-dealers, Reporting and recordkeeping requirements, Securities.

In accordance with the foregoing, Title 17, Chapter II of the Code of Federal Regulations is proposed to be amended as follows:

PART 240—GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE ACT OF 1934

1. The authority citation for part 240 continues to read in part 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, 78*l*, 78m, 78n, 78o, 78p, 78q, 78s, 78u–5, 78w, 78x, 78*ll*, 78mm, 80a–20, 80a–23, 80a–29, 80a–37, 80b–3, 80b–4, 80b–11 and 7201 *et seq.*; and 18 U.S.C. 1350, unless otherwise noted.

* * * * *

2. Revise § 240.15a–6 to read as follows:

§ 240.15a–6 Exemption of certain foreign brokers or dealers.

(a) A foreign broker or dealer shall be exempt from the registration requirements of sections 15(a)(1) and 15B(a)(1) of the Act and the reporting and other requirements of the Act (other than sections 15(b)(4) and 15(b)(6)), and the rules and regulations thereunder, that apply specifically to a broker or dealer that is not registered with the Commission solely by virtue of its status as a broker or dealer, with respect to a particular transaction or solicitation, to the extent that the foreign broker or dealer operates in compliance with paragraph (a)(1), (a)(2), (a)(3), (a)(4) or (a)(5) of this section with respect to such transaction or solicitation.

(1) *Unsolicited trades*. The foreign broker or dealer effects transactions in securities with or for persons that have not been solicited by the foreign broker or dealer.

(2) *Research reports*. The foreign broker or dealer furnishes research reports to qualified investors, and effects transactions in the securities discussed in the research reports with or for those qualified investors, provided that the following conditions are satisfied:

(i) The research reports do not recommend the use of the foreign broker or dealer to effect trades in any security;

(ii) The foreign broker or dealer does not initiate contact with those qualified investors to follow up on the research reports, and does not otherwise induce or attempt to induce the purchase or sale of any security by those qualified investors;

(iii) If the foreign broker or dealer has a relationship with a registered broker or dealer that satisfies the requirements of paragraph (a)(3) of this section, any transactions with the foreign broker or dealer in securities discussed in the research reports are effected pursuant to the provisions of paragraph (a)(3) of this section; and

(iv) The foreign broker or dealer does not provide research to U.S. persons pursuant to any express or implied understanding that those U.S. persons will direct commission income to the foreign broker or dealer.

(3) *Solicited trades*. The foreign broker or dealer induces or attempts to induce the purchase or sale of any security by a qualified investor, provided that the following conditions are satisfied:

(i) The foreign broker or dealer:

(A) Provides the Commission (upon request or pursuant to agreements reached between any foreign securities authority and the Commission or the U.S. government) with any information or documents within the possession, custody, or control of the foreign broker or dealer, any testimony of foreign associated persons, and any assistance in taking the evidence of other persons, wherever located, that the Commission requests and that relates to transactions under paragraph (a)(3) of this section, except that if, after the foreign broker or dealer has exercised its best efforts to provide the information, documents, testimony, or assistance, including requesting the appropriate governmental body and, if legally necessary, its customers (with respect to customer information) to permit the foreign broker or dealer to provide the information, documents, testimony, or assistance to the Commission, the foreign broker or dealer is prohibited from providing this information, documents, testimony, or assistance by applicable foreign law or regulations, then this paragraph (a)(3)(i)(A) shall not apply and the foreign broker or dealer will be subject to paragraph (c) of this section;

(B) Determines that the foreign associated person of the foreign broker or dealer effecting transactions with the qualified investor is not subject to a statutory disqualification specified in section 3(a)(39) of the Act;

(C) Has in its files, and will make available upon request by a registered broker or dealer satisfying the requirements described in paragraph (a)(3)(iii) of this section or the Commission, the types of information specified in § 240.17a–3(a)(12), provided that the information required by paragraph (a)(12)(i)(D) of § 240.17a–3 shall include sanctions imposed by foreign securities authorities, foreign exchanges, or foreign associations, including without limitation those described in section 3(a)(39) of the Act; and

(D) Discloses to the qualified investor:

(*1*) That the foreign broker or dealer is regulated by a foreign securities authority and not by the Commission; and

(*2*) Solely when the foreign broker or dealer is relying on paragraph (a)(3)(iii)(A)(*1*) of this section, that U.S. segregation requirements, U.S. bankruptcy protections and protections under the Securities Investor Protection Act will not apply to any funds or securities held by the foreign broker or dealer;

(ii) The foreign associated person of the foreign broker or dealer effecting transactions with the qualified investor conducts all securities activities from outside the United States, except that the foreign associated person may conduct visits to qualified investors within the United States, provided that transactions in any securities discussed during visits by the foreign associated person with qualified investors are effected pursuant to paragraph (a)(3) of this section; and

(iii) A registered broker or dealer:

(A) Is responsible for either:

(*1*) Maintaining copies of all books and records, including confirmations and statements issued by the foreign broker or dealer to the qualified investor, relating to any resulting transactions, except that such books and records may be maintained:

(*i*) In the form, manner and for the periods prescribed by the foreign securities authority regulating the foreign broker or dealer; and

(*ii*) With the foreign broker or dealer, provided that the registered broker or dealer makes a reasonable determination that copies of any or all of such books and records can be furnished promptly to the Commission, and promptly provides to the Commission any such books and records, upon request; or

(*2*) (*i*) Maintaining books and records, including copies of all confirmations issued by the foreign broker or dealer to the qualified investor, relating to any resulting transactions; and

(*ii*) Receiving, delivering and safeguarding funds and securities in connection with the transactions on behalf of the qualified investor in compliance with § 240.15c3–3;

(B) Obtains from the foreign broker or dealer and each foreign associated person written consent to service of process for any civil action brought by or proceeding before the Commission or a self-regulatory organization (as defined in section 3(a)(26) of the Act), providing that process may be served on them by service on the registered broker or dealer in the manner set forth on the registered broker's or dealer's current Form BD (17 CFR 249.501);

(C) Obtains from the foreign broker or dealer a representation that the foreign broker or dealer has complied with the requirements of paragraphs (a)(3)(i)(B) and (C) of this section; and

(D) Maintains records of the written consents required by paragraph (a)(3)(iii)(B) and the representations required by paragraph (a)(3)(iii)(C) of this section, and makes these records available to the Commission upon request.

(4) *Counterparties and specific customers.* The foreign broker or dealer effects transactions in securities with or for, or induces or attempts to induce the purchase or sale of any security by:

(i) A registered broker or dealer, whether the registered broker or dealer is acting as principal for its own account or as agent for others, or a bank acting pursuant to an exception or exemption from the definition of ''broker'' or ''dealer'' in section 3(a)(4)(B), 3(a)(4)(E), or 3(a)(5)(C) of the Act or the rules thereunder;

(ii) The African Development Bank, the Asian Development Bank, the Inter-American Development Bank, the International Bank for Reconstruction and Development, the International Monetary Fund, the United Nations and their agencies, affiliates and pension funds;

(iii) A foreign person temporarily present in the United States, with whom the foreign broker or dealer had a bona fide, pre-existing relationship before the foreign person entered the United States;

(iv) Any agency or branch of a U.S. person permanently located outside the United States, provided that the transactions occur outside the United States;

(v) U.S. citizens resident outside the United States, provided that the transactions occur outside the United States, and that the foreign broker or dealer does not direct its selling efforts toward identifiable groups of U.S. citizens resident abroad; or

(vi) Any U.S. person, other than a registered broker or dealer or a bank acting pursuant to an exception or exemption from the definition of ''broker'' or ''dealer'' in section 3(a)(4)(B), 3(a)(4)(E), or 3(a)(5)(C) of the Act or the rules thereunder, that acts in a fiduciary capacity for an account of a foreign resident client, provided the foreign broker or dealer:

(A) Only effects transactions in securities with or for, or induces or attempts to induce the purchase or sale of securities by, the U.S. person in the U.S. person's capacity as a fiduciary to an account of a foreign resident client; and

(B) Obtains and maintains a representation from the U.S. person that the account is managed in a fiduciary capacity for a foreign resident client.

(5) *Familiarization with foreign options exchanges.* The foreign broker or dealer effects transactions in options on foreign securities listed on a foreign options exchange of which it is a member for a qualified investor that has not been solicited by the foreign broker or dealer, except that:

(i) A representative of the foreign options exchange located in a foreign office or a representative office in the United States may:

(A) Communicate with persons that the representative of the foreign options exchange reasonably believes are qualified investors, including through participation in programs and seminars in the United States, regarding the foreign options exchange, the options on foreign securities traded on the foreign options exchange and, if applicable, the foreign options exchange's OTC options processing service;

(B) Provide persons that the representative of the foreign options exchange reasonably believes are qualified investors with a disclosure document that provides an overview of the foreign options exchange and the options on foreign securities traded on that exchange, including the differences from standardized options in the U.S. options market and special factors relevant to transactions by U.S. persons in options on the foreign options exchange; and

(C) Make available to persons that the representative of the foreign options exchange reasonably believes are qualified investors, solely upon request of the investor, a list of participants on the foreign options exchange permitted to take orders from the public and any registered broker or dealer affiliates of such participants;

(ii) The foreign broker or dealer may:

(A) Make available to qualified investors the foreign options exchange's OTC options processing service; and

(B) Provide qualified investors, in response to an unsolicited inquiry concerning options on foreign securities traded on the foreign options exchange, with a disclosure document that provides an overview of the foreign options exchange and the options on foreign securities traded on that exchange, including the differences from standardized options in the U.S. domestic options market and special factors relevant to transactions by U.S. persons in options on that exchange; and

(iii) The foreign exchange may make available to qualified investors through the foreign broker or dealer the foreign options exchange's OTC options processing service.

(b) *Definitions.* When used in this section:

(1) The term *foreign associated person* shall mean any natural person domiciled outside the United States who is an associated person, as defined in section 3(a)(18) of the Act, of the foreign broker or dealer and who participates in the solicitation of a qualified investor under paragraph (a)(3) of this section.

(2) The term *foreign broker or dealer* shall mean any non-U.S. resident person (including any U.S. person engaged in business as a broker or dealer entirely outside the United States, except as otherwise permitted by this section) that is not an office or branch of, or a natural person associated with, a registered broker or dealer, whose securities activities, if conducted in the United States, would be those of a ''broker'' or ''dealer,'' as defined in section 3(a)(4) or 3(a)(5) of the Act, and that:

(i) Solely for purposes of paragraph (a)(3) of this section, is regulated for conducting securities activities, including the specific activities in which the foreign broker or dealer engages with the qualified investor, in a foreign country by a foreign securities authority; and

(ii) Solely for purposes of paragraphs (a)(3)(iii)(A)(*1*) and (a)(4)(vi) of this section, conducts a foreign business.

(3) The term *foreign business* shall mean the business of a foreign broker or dealer with qualified investors and foreign resident clients where at least 85% of the aggregate value of the securities purchased or sold in transactions conducted pursuant to both paragraphs (a)(3) and (a)(4)(vi) of this section by the foreign broker or dealer

calculated on a rolling two-year basis is derived from transactions in foreign securities, except that the foreign broker or dealer may rely on the calculation made for the prior year for the first 60 days of a new year.

(4) The term *foreign resident client* shall mean:

(i) Any entity not organized or incorporated under the laws of the United States and not engaged in a trade or business in the United States for federal income tax purposes;

(ii) Any natural person not a U.S. resident for federal income tax purposes; and

(iii) Any entity not organized or incorporated under the laws of the United States 85 percent or more of whose outstanding voting securities are beneficially owned by persons in paragraphs (b)(4)(i) and (b)(4)(ii) of this section.

(5) The term *foreign security* shall mean:

(i) An equity security (as defined in 17 CFR 230.405) of a foreign private issuer (as defined in 17 CFR 230.405);

(ii) A debt security (as defined in 17 CFR 230.902) of a foreign private issuer (as defined in 17 CFR 230.405);

(iii) A debt security (as defined in 17 CFR 230.902) issued by an issuer organized or incorporated in the United States in connection with a distribution conducted solely outside the United States pursuant to Regulation S (17 CFR 230.903);

(iv) A security that is a note, bond, debenture or evidence of indebtedness issued or guaranteed by a foreign government (as defined in 17 CFR 230.405) that is eligible to be registered with the Commission under Schedule B of the Securities Act of 1933; and

(v) A derivative instrument on a security described in paragraph (b)(5)(i), (b)(5)(ii), (b)(5)(iii), or (b)(5)(iv) of this section.

(6) The term *OTC options processing service* shall mean a mechanism for submitting an options contract on a foreign security that has been negotiated and completed in an over-the-counter transaction to a foreign options exchange so that the foreign options exchange may replace that contract with an equivalent standardized options contract that is listed on the foreign options exchange and that has the same terms and conditions as the over-the-counter options.

(7) The term *registered broker or dealer* shall mean a person that is registered with the Commission under section 15(b), 15B(a)(2), or 15C(a)(2) of the Act.

(8) The term *United States* shall mean the United States of America, including the States and any territories and other areas subject to its jurisdiction.

(c) *Withdrawal of exemption.* The Commission, by order after notice and opportunity for hearing, may withdraw the exemption provided in paragraph (a)(3) of this section with respect to the subsequent activities of a foreign broker or dealer or class of foreign brokers or dealers conducted from a foreign country, if the Commission finds that the laws or regulations of that foreign country have prohibited the foreign broker or dealer, or one of a class of foreign brokers or dealers, from providing, in response to a request from the Commission, information or documents within its possession, custody, or control, testimony of foreign associated persons, or assistance in taking the evidence of other persons, wherever located, related to activities exempted by paragraph (a)(3) of this section.

Dated: June 27, 2008.

By the Commission.

Florence E. Harmon,

Acting Secretary.

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