maturity of grapefruit imported into the United States. * * *

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Dated: October 15, 2018.

Bruce Summers,

Administrator, Agricultural Marketing Service.

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SECURITIES AND EXCHANGE COMMISSION

17 CFR Part 240

[Release No. 34–84409; File No. S7–08–12]

RIN 3235–AL12

Capital, Margin, and Segregation Requirements for Security-Based Swap Dealers and Major Security-Based Swap Participants and Capital Requirements for Broker-Dealers

AGENCY: Securities and Exchange Commission.

ACTION: Proposed rule; reopening of comment period; request for additional comment.

SUMMARY: The Securities and Exchange Commission (''Commission'') is reopening the comment period and requesting additional comment (including potential modifications to proposed rule language) on the following: Proposed amendments and new rules that would establish capital and margin requirements for security-based swap dealers (''SBSDs'') and major security-based swap participants (''MSBSPs'') that do not have a prudential regulator, establish segregation requirements for SBSDs, establish notification requirements for SBSDs and MSBSPs relating to segregation, and raise minimum net capital requirements and establish liquidity requirements for broker-dealers permitted to use internal models when computing net capital (''ANC broker-dealers''). The Commission also is reopening the comment period and requesting additional comment on proposed amendments that would establish the cross-border treatment of security-based swap capital, margin, and segregation requirements; and a proposed amendment that would establish an additional capital requirement for SBSDs that do not have a prudential regulator.

DATES: The comment periods for portions of the proposed rules published Nov. 23, 2012 (77 FR 70213); May 23, 2013 (78 FR 30967); and May 2, 2014 (79 FR 25193), are reopened. Comments should be submitted by November 19, 2018.

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/other.shtml*); or
- Send an email to *rule-comments@sec.gov*. Please include File No. S7–08–12 on the subject line.

Paper Comments

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

All submissions should refer to File Number S7–08–12. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method of submission. The Commission will post all comments on the Commission's website (*http://www.sec.gov*). Comments are also available for website viewing and printing in the Commission's Public Reference Room, 100 F Street NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make publicly available.

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

FOR FURTHER INFORMATION CONTACT: Michael A. Macchiaroli, Associate Director, at (202) 551–5525; Thomas K. McGowan, Associate Director, at (202) 551–5521; Randall W. Roy, Deputy Associate Director, at (202) 551–5522; Sheila Dombal Swartz, Senior Special Counsel, at (202) 551–5545; Timothy C. Fox, Branch Chief, at (202) 551–5687; Valentina Minak Deng, Special Counsel, at (202) 551–5778; or Nina Kostyukovsky, Attorney Advisor, at (202) 551–8833, Division of Trading and Markets, Securities and Exchange Commission, 100 F Street NE, Washington, DC 20549–7010.

SUPPLEMENTARY INFORMATION:

I. Background

In October 2012, the Commission proposed amendments and new rules to: (1) Establish capital and margin requirements for SBSDs and MSBSPs that do not have a prudential regulator [1] (''nonbank SBSDs'' and ''nonbank MSBSPs'', respectively); (2) establish segregation requirements for SBSDs; (3) establish notification requirements for SBSDs and MSBSPs relating to segregation; and (4) raise minimum net capital requirements and establish liquidity requirements for ANC broker-dealers.[2] The Commission published the *2012 Proposals* largely pursuant to Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (''Title VII of the Dodd-Frank Act''). The Commission extended the comment period once,[3] and reopened it once.[4] The Commission has received a number of comment letters in response to the *2012 Proposals.*[5]

In addition, in May 2013, the Commission proposed provisions to establish the cross-border treatment of security-based swap capital, margin, and segregation requirements.[6] The

[1] The term ''prudential regulator'' is defined in Section 1(a)(39) of the Commodity Exchange Act (7 U.S.C. 1(a)(39)) and that definition is incorporated by reference in Section 3(a)(74) of the Securities Exchange Act of 1934 (''Exchange Act'' or ''Act''). 15 U.S.C. 78c(a)(74). Pursuant to the definition, the Board of Governors of the Federal Reserve System (''FRB''), the Office of the Comptroller of the Currency (''OCC''), the Federal Deposit Insurance Corporation (''FDIC''), the Farm Credit Administration (''FCA''), or the Federal Housing Finance Agency (''FHFA'') (collectively, the ''prudential regulators'') is the ''prudential regulator'' of an SBSD, MSBSP, swap participant, or major swap participant if the entity is directly supervised by that agency.

[2] *See Capital, Margin, and Segregation Requirements for Security-Based Swap Dealers and Major Security-Based Swap Participants and Capital Requirements for Broker-Dealers,* Exchange Act Release No. 68071 (Oct. 18, 2012), 77 FR 70214 (Nov. 23, 2012) (''*2012 Proposals*'').

[3] *See Capital, Margin, and Segregation Requirements for Security-Based Swap Dealers and Major Security-Based Swap Participants and Capital Requirements for Broker-Dealers,* Exchange Act Release No. 68660 (Jan. 15. 2013), 78 FR 4365 (Jan. 22, 2013).

[4] *See Reopening of Comment Periods for Certain Rulemaking Releases and Policy Statement Applicable to Security-Based Swaps Proposed Pursuant to the Securities Exchange Act of 1934 and the Dodd-Frank Wall Street Reform and Consumer Protection Act,* Exchange Act Release No. 69491 (May 1, 2013), 78 FR 30800 (May 23, 2013).

[5] The comment letters are available at *http://www.sec.gov/comments/s7-08-12/s70812.shtml.*

[6] *See Cross-Border Security-Based Swap Activities; Re-Proposal of Regulation SBSR and Certain Rules and Forms Relating to the Registration of Security-Based Swap Dealers and*

Continued

Commission has received a number of comment letters in response to the *2013 Proposals.*[7]

Finally, in April 2014, the Commission proposed an additional nonbank SBSD capital requirement.[8] The Commission has received one comment letter in response to the *2014 Proposal.*[9]

In the releases publishing the *Proposals,* the Commission described the statutory and regulatory background for the proposed amendments and rules, the rationales for each of the proposed amendments and rules, the potential economic consequences, including the baseline against which the proposed amendments and rules may be evaluated, the potential costs and benefits, reasonable alternatives, and the potential effects on efficiency, competition, and capital formation.[10]

Since publication of the *2012 Proposals,* the Commission has adopted other rules relating to the regulation of the over-the-counter derivatives markets pursuant to Title VII of the Dodd-Frank Act.[11] In addition, the prudential regulators and the Commodity Futures Trading Commission (''CFTC'') have adopted or proposed rules under Title VII of the Dodd-Frank Act that are relevant to the *Proposals.*[12]

The Commission has carefully considered the comment letters, and the Commission believes it is prudent to reopen the comment period for the *Proposals* in light of these comments and regulatory developments. In addition, the Commission believes the public should have the opportunity to provide comment on the potential economic effects of the *Proposals* in light of regulatory and market developments since they were published. Accordingly, the Commission is reopening the public comment period for 30 days and seeking comment on all aspects of the *Proposals.* The Commission also is seeking specific comment on certain aspects of the *Proposals* where further information would be particularly helpful to the Commission. In particular, the Commission is seeking comment on potential rule language that would modify rule text that was in the *Proposals.* This modified rule language would be included in: (1) Existing rules 17 CFR 240.15c3–1 (''Rule 15c3–1''), 17 CFR 240.15c3–1a (''Appendix A to Rule 15c3–1''), 17 CFR 240.15c3–3 (''Rule 15c3–3''), and 17 CFR 240.3a71–6 (''Rule 3a71–6''); (2) new rule 17 CFR 240.15c3–3b (''Exhibit B to Rule 15c3–3''); and (3) in proposed rules 17 CFR 240.18a–1 (''Rule 18a–1''), 17 CFR 240.18a–1a (''Appendix A to Rule 18a–1''), 17 CFR 240.18a–3 (''Rule 18a–3''), 17 CFR 240.18a–4 (''Rule 18a–4''), and 17 CFR 240.18a–4a (''Exhibit A to Rule 18a–4''). Comment letters received by the Commission previously need not be re-submitted as they will continue to be a part of the public comment file for this rulemaking and considered by the Commission.

II. Request for Comment

The Commission renews its request for comment on all aspects of the *Proposals* and on the specific topics identified below. Commenters are requested to provide empirical data in support of any arguments and analyses. The Commission notes that comments are of the greatest assistance to rulemaking initiatives when accompanied by supporting data and analysis, and, if appropriate, accompanied by alternative approaches and suggested language.

Capital

1. The *2012 Proposals* included a provision that would establish a financial ratio-derived minimum net capital requirement for a nonbank SBSD equal to eight percent (8%) of the firm's *risk margin amount.*[13] The *risk margin amount* would be the sum of:

- The greater of the total margin required to be delivered by the nonbank SBSD with respect to security-based swap transactions cleared for security-based swap customers at a clearing agency or the amount of the deductions (haircuts) that would apply to the cleared security-based swap positions of the security-based swap customers pursuant to the proposed capital requirements; and
- The total margin amount calculated by the nonbank SBSD with respect to non-cleared security-based swaps pursuant to the proposed margin rule.[14]

The total of these two amounts would be multiplied by eight percent (8%) to determine the dollar amount of this ratio requirement (and the nonbank SBSD's minimum net capital requirement would be the greater of a

Major Security-Based Swap Participants, Exchange Act Release No. 69490 (May 1, 2013), 78 FR 30968 (May 23, 2013) (''*2013 Proposals*'').

[7] The comment letters are available at *http://www.sec.gov/comments/s7-02-13/s70213.shtml.*

[8] *See Recordkeeping and Reporting Requirements for Security-Based Swap Dealers, Major Security-Based Swap Participants, and Broker-Dealers; Capital Rule for Certain Security-Based Swap Dealers,* Exchange Act Release No. 71958 (Apr. 17, 2014), 79 FR 25194, 25254 (May 2, 2014) (the ''*2014 Proposal*'' and together with the *2012 Proposals* and the *2013 Proposals,* the ''*Proposals*'').

[9] The comment letter is available at: *https://www.sec.gov/comments/s7-05-14/s70514.shtml.*

[10] *See Proposals.*

[11] *See Clearing Agency Standards,* Exchange Act Release No. 68080 (Oct. 22, 2012), 77 FR 66220 (Nov. 11, 2012); *Application of* ''*Security-Based Swap Dealer*'' *and* ''*Major Security-Based Swap Participant*'' *Definitions to Cross-Border Security-Based Swap Activities,* Exchange Act Release No. 72472 (June 25, 2014), 79 FR 47278 (Aug. 12, 2014); *Regulation SBSR—Reporting and Dissemination of Security-Based Swap Information,* Exchange Act Release No. 74244 (Feb. 11, 2015), 80 FR 14563 (Mar. 19, 2015); *Security-Based Swap Data Repository Registration, Duties, and Core Principles,* Exchange Act Release No. 74246 (Feb. 11, 2015), 80 FR 14437 (Mar. 19, 2015); *Registration Process for Security-Based Swap Dealers and Major Security-Based Swap Participants,* Exchange Act Release No. 75611 (Aug. 5, 2015), 80 FR 48963 (Aug. 14, 2015); *Security-Based Swap Transactions Connected with a Non-U.S. Person's Dealing Activity That Are Arranged, Negotiated, or Executed By Personnel Located in a U.S. Branch or Office or in a U.S. Branch or Office of an Agent; Security-Based Swap Dealer De Minimis Exception,* Exchange Act Release No. 77104 (Feb. 10, 2016), 81 FR 8597 (Feb. 19, 2016); *Business Conduct Standards for Security-Based Swap Dealers and Major Security-Based Swap Participants,* Exchange Act Release No. 77617 (Apr. 14, 2016), 81 FR 29960 (May 13, 2016); *Trade Acknowledgment and Verification of Security-Based Swap Transactions,* Exchange Act Release No. 78011 (June 8, 2016), 81 FR 39808 (June 17, 2016); *Regulation SBSR—Reporting and Dissemination of Security-Based Swap Information,* Exchange Act Release No. 78321 (July 14, 2016), 81 FR 53545 (Aug. 12, 2016); *Access to Data Obtained by Security-Based Swap Data Repositories,* Exchange Act Release No. 78716 (Aug. 29, 2016), 81 FR 60585 (Sept. 2, 2016).

[12] *See* FRB, OCC, FDIC, FCA, FHFA, *Margin and Capital Requirements for Covered Swap Entities,* 80 FR 74840 (Nov. 30, 2015) (adopting capital and margin requirements for bank swap dealers, bank SBSDs, bank swap participants, and bank MSBSPs); CFTC, *Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants,* 81 FR 636 (Jan. 6, 2016) (adopting margin requirements for nonbank swap dealers and nonbank major swap participants); CFTC, *Capital Requirements of Swap Dealers and Major Swap Participants,* 81 FR 91252 (Dec. 16, 2016) (proposing capital requirements for nonbank swap dealers and nonbank major swap participants).

[13] *See 2012 Proposals,* 77 FR at 70223–24. Minimum net capital requirements would be the greater of a fixed-dollar amount and an amount derived by applying a financial ratio. *See id.* at 70221.

[14] The ratio-based minimum net capital calculation shown as an equation would be: $MRNC = [\max(IM^C, HC^C) + IM^{NC}] \times 8\%$. Where MRNC is the ratio-based minimum net capital requirement, IM^C is the amount of initial margin for cleared security-based swaps, HC^C is the amount of haircuts applied to the same cleared security-based swaps, IM^{NC} is the amount of initial margin calculated for non-cleared security-based swaps, and $(\max(IM^C, HC^C) + IM^{NC})$ is the *risk margin amount.* For example, assume that IM^C is $10, HC^C is $15, and IM^{NC} is $25. In this simple hypothetical example, the *risk margin amount* would equal $40 [max($10, $15) + $25], and the ratio-based minimum net capital requirement would be $3.20 ($40 × 8%). As proposed, a stand-alone nonbank SBSD would be subject to this ratio-based minimum net capital requirement, whereas a nonbank SBSD dually registered as a broker-dealer would be subject to the sum of this ratio-based minimum net capital requirement plus one of the two existing financial ratio-based minimum net capital requirements in Rule 15c3–1.

fixed-dollar amount and a ratio amount). The proposal for a ratio amount relating to security-based swaps was designed to establish a minimum net capital requirement that increases in tandem with an increase in the risks associated with a nonbank SBSD's security-based swap activities. This scaled ratio amount is separate from the fixed-dollar amount that sets a floor to the minimum net capital requirement.[15]

a. The Commission requests comment and supporting data on the potential minimum net capital amounts that would be required of nonbank SBSDs as a result of the requirement, as proposed. How would those potential minimum net capital amounts compare with the amounts of capital currently maintained by entities that may register as nonbank SBSDs?

b. One commenter suggested that the Commission modify its proposed definition of the *risk margin amount* to reflect the lower risk associated with central clearing.[16] In light of the comment and the goals of this provision, the Commission requests comment on whether the input to the *risk margin amount* for cleared security-based swaps should be modified. Should the input to the *risk margin amount* for cleared security-based swaps be determined solely by the total initial margin required to be delivered by the nonbank SBSD with respect to security-based swap transactions cleared for security-based swap customers at a clearing agency (*i.e.,* not be the greater of that amount or the amount of the deductions (haircuts) that would apply to the cleared security-based swap positions)?[17] The purpose of this potential modification would be to simplify the calculation, align it with the clearing agency margin requirements, and more closely align it with the CFTC's existing rules and proposals.[18]

Would rule language as described below effect this potential modification to the rule text in the *2012 Proposals*? If not, please explain why and suggest alternative rule language. If the Commission were to use the language described below, would it strike an appropriate balance in terms of achieving the objectives of the proposed rule and addressing the commenter's concern described above? If not, please explain why and suggest alternative rule language that could more effectively and efficiently strike the balance and achieve the objective.

The potential modifications to paragraph (c)(17) of Rule 15c3–1 would provide that the term *risk margin amount* means the sum of: (i) The total initial margin required to be maintained by the broker or dealer at each clearing agency with respect to security-based swap transactions cleared for security-based swap customers; and (ii) the total margin amount calculated by the broker or dealer with respect to non-cleared security-based swaps pursuant to § 240.18a–3(c)(1)(i)(B).

Similarly, the potential modifications to paragraph (c)(6) of Rule 18a–1 would provide that the term *risk margin amount* means the sum of: (i) The total initial margin required to be maintained by the security-based swap dealer at each clearing agency with respect to security-based swap transactions cleared for security-based swap customers; and (ii) the total margin amount calculated by the security-based swap dealer with respect to non-cleared security-based swaps pursuant to § 240.18a–3(c)(1)(i)(B).

2. The *2012 Proposals* included a capital charge that would apply if a nonbank SBSD collects an amount of margin from a counterparty to a cleared security-based swap that is less than the deduction that would apply to the security-based swap if it was a proprietary position of the firm.[19] This proposed requirement was designed to account for the risk of the counterparty defaulting by requiring the nonbank SBSD to maintain capital in the place of margin in an amount that is no less than would be required for a proprietary position.[20] It also was designed to ensure that there is a standard minimum coverage for exposure to cleared security-based swap counterparties apart from the individual clearing agency margin requirements, which could vary among clearing agencies and over time.[21]

One commenter opposed this proposal stating that the requirement would ''harm customers because it would provide an incentive for the collection of margin by nonbank SBSDs beyond the amount determined by the clearing agency.''[22] In light of the comment and the goals of this provision, the Commission requests comment on whether this proposed capital charge should be modified to include a risk-based threshold under which the proposed capital charge need not be taken. Should the rule provide that the deduction need not be taken if the difference between the clearing agency margin amount and the haircut is less than one percent (1%) or some other percent of the nonbank SBSD's tentative net capital[23] and less than ten percent (10%) or some other percent of the counterparty's net worth,[24] and the aggregate difference across all counterparties is less than twenty-five percent (25%) or some other percent of the nonbank SBSD's tentative net capital?[25] The purpose of these thresholds would be to limit the nonbank SBSD's exposure to a single counterparty as well as to establish a concentration limit across all counterparties. In addition, these thresholds would be scalable and have a more direct relation to the risk to the nonbank SBSD arising from its security-based swap activities.

Would rule language as described below effect this potential modification

[15] *See id.* at 70223–24.

[16] *See* Letter from Stuart J. Kaswell, Executive Vice President, Managing Director, and General Counsel, Managed Funds Association (Feb. 22, 2013).

[17] The ratio-based minimum net capital calculation shown as an equation would be: MRNC = $(IM^{C} + IM^{NC}) \times 8\%$.

[18] Eliminating the haircut input to the *risk margin amount* for cleared security-based swaps would more closely align it with the CFTC's existing rules and proposals. For example, currently futures commission merchants (''FCMs'') registered with the CFTC must maintain adjusted net capital in excess of eight percent (8%) of the risk margin on futures, foreign futures, and cleared swaps positions carried in customer and noncustomer accounts. *See* 17 CFR 1.17. The CFTC has proposed a similar requirement for swap dealers registered as FCMs that also would generally include in the FCM's minimum net capital requirement eight percent (8%) of the total initial margin an FCM is required to post to a clearing agency for cleared security-based swap positions (as well as the initial margin on uncleared swap and security-based swap positions for which the FCM is a counterparty). *See Capital Requirements of Swap Dealers and Major Swap Participants,* 81 FR at 91266.

[19] *See 2012 Proposals,* 77 FR at 70245–46.

[20] *See id.* at 70246.

[21] *See id.*

[22] *See* Letter from Kenneth E. Bentsen, Jr., Executive Vice President, Securities Industry and Financial Markets Association (Feb. 22, 2013) (''*SIFMA 2/22/2013 Letter*'').

[23] *See, e.g., Order Granting Conditional Exemption Under the Securities Exchange Act of 1934 in Connection with Portfolio Margining of Swaps and Security-Based Swaps,* Exchange Act Release No. 68433 (Dec. 14, 2012), 77 FR 75211 (Dec. 19, 2012). Pursuant to this order, Commission staff granted conditional temporary approval to certain broker-dealers that are also registered as FCMs to participate in a credit default swap (CDS) portfolio margining program, subject to specified conditions. One condition requires a firm to calculate its net credit exposure to a client and if the client's net credit exposure is in excess of one percent (1%) of the firm's tentative net capital, the firm is required to either collect the net credit exposure above the one percent (1%) threshold in the form of margin from its client or take a capital charge equal to that amount. *See, e.g.,* Letter to Keith Bailey, Barclays Capital Inc. from Michael A. Macchiaroli, Division of Trading and Markets, Commission (June 7, 2013).

[24] *See, e.g.,* 17 CFR 240.15c3–1(c)(2)(vi)(M)(*1*) (using a ten percent (10%) of tentative net capital threshold for the calculation of undue concentration charges).

[25] *See, e.g.,* 17 CFR 240.15c3–3a, Note E(5) (using a twenty-five percent (25%) of tentative net capital threshold for when a broker-dealer must reduce debits in the customer reserve formula).

to the rule text in the *2012 Proposals*? If not, please explain why and suggest alternative rule language. If the Commission were to use the language described below, would it strike an appropriate balance in terms of achieving the objectives of the proposed rule and addressing the commenter's concern described above? If not, please explain why and suggest alternative rule language that could more effectively and efficiently strike the balance and achieve the objective.

The potential modifications to paragraph (c)(2)(xv)(A) of Rule 15c3–1 would provide the following deduction from net worth in lieu of collecting collateral for cleared security-based swaps and swap transactions: (*1*) Deducting the amount of the margin difference for each account carried by the broker or dealer for another person that holds cleared security-based swap or swap transactions. The margin difference is the amount of the deductions to the positions in the account calculated pursuant to paragraph (c)(2)(vi) of this section, § 240.15c3–1b, or § 240.15c3–1e (as applicable), less the margin value of collateral held in the account. (*2*) *Exception.* The deduction required pursuant to paragraph (c)(2)(xv)(A)(*1*) of this section need not be taken to the extent that: (*i*) The amount of the margin difference for the account does not exceed the lesser of 1 percent (1%) of the tentative net capital of the broker or dealer or ten percent (10%) of the net worth of the counterparty; and (*ii*) The amount of the margin difference for all accounts that hold security-based swaps or swaps does not exceed twenty-five percent (25%) of the tentative net capital of the broker or dealer.

Similarly, the potential modifications to paragraph (c)(1)(ix)(A) of Rule 18a–1 would provide the following deduction from net worth in lieu of collecting collateral for security-based swaps and swap transactions: (*1*) Deducting the amount of the margin difference for each account carried by the security-based swap dealer for another person that holds cleared security-based swap or swap transactions. The margin difference is the amount of the deductions to the positions in the account calculated pursuant to paragraph (c)(1)(vi) or (vii) of this section, § 240.18a–1(d), or § 240.18a–1b (as applicable), less the margin value of collateral held in the account. (*2*) *Exception.* The deduction required pursuant to paragraph (c)(1)(ix)(A)(*1*) of this section need not be taken to the extent that: (*i*) The amount of the margin difference for the account does not exceed the lesser of 1 percent (1%) of the tentative net capital of the security-based swap dealer or ten percent (10%) of the net worth of the counterparty; and (*ii*) The amount of the margin difference for all accounts that hold security-based swaps or swaps does not exceed twenty-five percent (25%) of the tentative net capital of the security-based swap dealer.

3. The *2012 Proposals* included a provision that a nonbank SBSD would be required to take a 100 percent (100%) capital charge when it does not collect variation or initial margin for non-cleared security-based swaps because of an exception from collecting margin.[26] The proposed capital charge was intended to require a nonbank SBSD to set aside net capital to address the risks that would otherwise be mitigated through the collection of variation and initial margin.[27] The set aside net capital would serve as an alternative to obtaining margin.[28] As an alternative to taking the 100 percent (100%) charge, the Commission proposed that firms using internal models to calculate net capital could take a credit risk charge if the uncollected margin involved a transaction with a commercial end user.[29]

a. Commenters requested that nonbank SBSDs be permitted to apply the credit risk charge to other types of counterparties.[30] In light of the comments and the goals of this provision, the Commission requests comment on whether the use of the credit risk charge should be expanded to other types of counterparties and transactions. Should the rule permit a firm to apply the credit risk charge for uncollected initial margin for security-based swaps and swap transactions with any type of counterparty and for uncollected variation margin for transactions with a commercial end user only? The purpose of limiting the application of the credit risk charge with respect to uncollected variation margin to transactions with commercial end users would be to reduce the types of unsecured receivables that qualify as allowable assets for net capital purposes and, thereby, promote the liquidity of the nonbank SBSD.

b. The Commission requests comment on whether the rule should establish a threshold for uncollected margin above which the use of the credit risk charge would not be permitted. Should there be a threshold when the aggregate amount of uncollected margin across all counterparties exceeds a level of the nonbank SBSD's tentative net capital? Should the threshold apply to the aggregate amount of uncollected initial *and* variation margin or just to the aggregate amount of uncollected variation margin? The latter approach would focus the threshold on unsecured receivables that result from not collecting variation margin and, thereby, promote the liquidity of the nonbank SBSD. Should there be a threshold with respect to uncollected variation margin for security-based swap and swap transactions with commercial end users and should that threshold be ten percent (10%) or some other percent of the nonbank SBSD's tentative net capital?[31] This threshold would be designed to limit the nonbank SBSD's aggregate exposure arising from not collecting variation margin from commercial end users and would be scalable to the nonbank SBSD's financial condition.

c. The potential modifications to the rule text in the *2012 Proposals* discussed above in 3.a and 3.b would include: (1) Changing the proposed rule to permit a nonbank SBSD to apply the credit risk charge for uncollected initial margin for security-based swaps and swaps from any type of counterparty and for uncollected variation margin from a commercial end user; and (2) establishing a risk-based threshold with respect to uncollected variation margin from commercial end users. Would rule language as described below effect this potential modification to the rule text in the *2012 Proposals*? If not, please explain why and suggest alternative rule language. If the Commission were to use the language described below, would it strike an appropriate balance in terms of achieving the objectives of the proposed rule and addressing commenters' requests to apply the credit risk charge more broadly? If not, please explain why and suggest alternative rule language that could more effectively and efficiently strike the balance and achieve the objective.

The potential modifications to paragraph (a)(7) of Rule 15c3–1 would provide: In accordance with Appendix E to this section (§ 240.15c3–1e), the Commission may approve, in whole or in part, an application or an amendment to an application by a broker or dealer to calculate net capital using the market risk standards of appendix E to compute a deduction for market risk on some or

[26] *See 2012 Proposals,* 77 FR at 70425–27.

[27] *See id.*

[28] *See id.*

[29] *See id.* at 70240–45.

[30] *See, e.g.,* Letter from Anne-Marie Leroy, Senior Vice President and Group General Counsel, and David Harris, Acting Vice President and General Counsel, The World Bank (Feb. 21, 2013).

[31] *See, e.g.,* 17 CFR 240.15c3–1(c)(2)(vi)(M)(*1*) (using a ten percent (10%) of tentative net capital threshold for the calculation of undue concentration charges).

all of its positions, instead of the provisions of paragraphs (c)(2)(vi) and (c)(2)(vii) of this section, and § 240.15c3–1b, and using the credit risk standards of Appendix E to compute a deduction for credit risk for certain security-based swap and swap transactions, as specified in this paragraph, instead of the provisions of paragraphs (c)(2)(iv), (c)(2)(xv)(B)(*1*), and (c)(2)(xv)(B)(*2*) of this section, subject to any conditions or limitations on the broker or dealer the Commission may require as necessary or appropriate in the public interest or for the protection of investors. A broker or dealer may use the credit risk standards of Appendix E to compute a deduction for credit risk for security-based swap transactions with *commercial end users* as that term is defined in § 240.18a–3(b)(2), and swap transactions in which a counterparty qualifies for an exception from margin requirements pursuant to Section 4s(e)(4) of the Commodity Exchange Act (7 U.S.C. 6s(e)(4)) instead of the provisions of paragraph (c)(2)(iv) of this section, provided that the deductions, in the aggregate, do not exceed ten percent (10%) of the tentative net capital of the broker or dealer. A broker or dealer also may use the credit risk standards of Appendix E to compute a deduction for credit risk for security-based swap transactions that are subject to an initial margin exception set forth in § 240.18a–3(c)(1)(iii) instead of the provisions of paragraph (c)(2)(xv)(B)(*1*) of this section, and for swap transactions instead of the provisions of paragraph (c)(2)(xv)(B)(*2*) of this section.

Similarly, the potential modifications to paragraph (a)(2) of Rule 18a–1 would provide: In accordance with paragraph (d) of this section, the Commission may approve, in whole or in part, an application or an amendment to an application by a security-based swap dealer to calculate net capital using the market risk standards of paragraph (d) to compute a deduction for market risk on some or all of its positions, instead of the provisions of paragraphs (c)(1)(iv), (vi), and (vii) of this section, and § 240.18a–1b, and using the credit risk standards of paragraph (d) to compute a deduction for certain security-based swap and swap transactions, as specified in this paragraph, instead of the provisions of paragraphs (c)(1)(iii), (c)(1)(ix)(B)(*1*), and (c)(1)(ix)(B)(*2*) of this section, subject to any conditions or limitations on the security-based swap dealer the Commission may require as necessary or appropriate in the public interest or for the protection of investors. A security-based swap dealer may use the credit risk standards of paragraph (d) to compute a deduction for credit risk for security-based swap transactions with *commercial end users* as that term is defined in § 240.18a–3(b)(2), and swap transactions in which a counterparty qualifies for an exception from margin requirements pursuant to Section 4s(e)(4) of the Commodity Exchange Act (7 U.S.C. 6s(e)(4)) instead of the provisions of paragraph (c)(1)(iii) of this section, provided that the deductions, in the aggregate, do not exceed ten percent (10%) of the tentative net capital of security-based swap dealer. A security-based swap dealer also may use the credit risk standards of paragraph (d) to compute a deduction for credit risk for security-based swap transactions that are subject to an initial margin exception set forth in § 240.18a–3(c)(1)(iii) instead of the provisions of paragraph (c)(1)(ix)(B)(*1*) of this section, and for swap transactions instead of the provisions of paragraph (c)(1)(ix)(B)(*2*) of this section.

4. The *2012 Proposals* included a capital charge for nonbank SBSDs when a counterparty requires initial margin to be segregated pursuant to Section 3E(f) of the Act, which among other things, provides that the collateral must be carried by an independent third-party custodian.[32] Collateral held in this manner would not be in the possession or control of the nonbank SBSD, nor would it would be capable of being liquidated promptly by the nonbank SBSD without the intervention of a third party.

a. Commenters argued that the charge would discourage the use of segregation under Section 3E(f) of the Act,[33] that the charge would create costs to the affected nonbank SBSD (which would be passed on to customers),[34] and that the parties could properly structure an agreement to address the Commission's concern about the nonbank SBSD's lack of control over the collateral.[35] In light of the comments and the goals of this provision, the Commission requests comment on whether there should be an exception to taking the capital charge (whether 100 percent (100%) or a credit risk charge, as applicable) under conditions that promote the SBSD's ability to promptly access the collateral if needed. Should there be an exception with the following conditions: (1) The custodian is a bank; (2) the nonbank SBSD enters into an agreement with the custodian and the counterparty that provides the nonbank SBSD with the same control over the collateral as would be the case if the nonbank SBSD controlled the collateral directly; and (3) an opinion of counsel deems the agreement enforceable? The purpose of these conditions would be to provide the nonbank SBSD with the unfettered ability to access the collateral in the event the counterparty defaults and, thereby, promote the financial condition of the nonbank SBSD, particularly in a time of market distress. Would this be a practical exception? If not, please explain why.

b. The Commission is considering providing guidance on ways a nonbank SBSD could structure the account control agreement to meet a requirement that the nonbank SBSD have the same control over the collateral as would be the case if the nonbank SBSD controlled the collateral directly. In developing the guidance on ways this requirement could be met, the Commission asks commenters to address whether the agreement between the nonbank SBSD, counterparty, and the third-party custodian should: (1) Provide that the collateral will be released promptly and directed in accordance with the instructions of the nonbank SBSD upon the receipt of an effective notice from the nonbank SBSD; (2) provide that when the counterparty provides an effective notice to access the collateral the nonbank SBSD will have sufficient time to challenge the notice in good faith and that the collateral will not be released until a prior agreed-upon condition among the three parties has occurred; and (3) give priority to an effective notice from the nonbank SBSD over an effective notice from the counterparty, as well as priority to the nonbank SBSD's instruction about how to transfer the collateral in the event the custodian terminates the account control agreement? Are there any other provisions regarding the account control agreement that the Commission should address to assist nonbank SBSDs in structuring the agreements to meet a requirement in a rule that the nonbank SBSD have the same control over the collateral as would be the case if the nonbank SBSD controlled the collateral directly?

c. The potential modification to the rule text in the *2012 Proposals*

[32] *See 2012 Proposals,* 77 FR at 70246–47; 15 U.S.C. 78c–5(f)(3).

[33] *See, e.g.,* Letter from American Benefits Council, Committee on Investment of Employee Benefit Assets, European Federation for Retirement Provision, the European Association of Paritarian Institutions, the National Coordinating Committee for Multiemployer Plans, and the Pension Investment Association of Canada (May 19, 2014).

[34] *See, e.g.,* Letter from Douglas M. Hodge, Managing Director and Chief Operating Officer, Pacific Investment Management Company LLC (Feb. 21, 2013).

[35] *See, e.g.,* Letter from Karrie McMillan, General Counsel, Investment Company Institute (Dec. 5, 2013).

discussed above in 4.a would establish conditions under which a nonbank SBSD could avoid the capital charge that applies when a counterparty requires initial margin to be segregated pursuant to Section 3E(f) of the Act. Would rule language as described below effect this potential modification to the rule text in the *2012 Proposals*? If not, please explain why and suggest alternative rule language. If the Commission were to use the language described below, would it strike an appropriate balance in terms of achieving the objectives of the proposed rule and addressing the commenters' concerns about the impact of the capital charge? If not, please explain why and suggest alternative rule language that could more effectively and efficiently strike the balance and achieve the objective.

The potential modifications to paragraph (c)(2)(xv)(B) of Rule 15c3–1 would provide the following deductions from net worth in lieu of collecting collateral for security-based swap and swap transactions: (*1*) *Security-based swaps.* Deducting the amounts calculated pursuant to § 240.18a–3(c)(1)(i)(B) for the account of a counterparty at the broker or dealer that is subject to an initial margin exception set forth in § 240.18a–3(c)(1)(iii), less the margin value of collateral held in the account of the counterparty at the broker or dealer. (*2*) *Swaps.* Deducting the initial margin calculated pursuant to § 240.18a–3(d)(2) for swaps other than equity swaps, or § 240.15c3–1b, as applicable, in the account of a counterparty at the broker or dealer, less the margin value of collateral held in the account of the counterparty at the broker or dealer. (*3*) *Treatment of collateral held at a third-party custodian.* For the purposes of the deductions required pursuant to paragraphs (c)(2)(xv)(B)(*1*) and (*2*) of this section, collateral held by an independent third-party custodian as initial margin pursuant to Section 3E(f) of the Act or Section 4s(l) of the Commodity Exchange Act may be treated as collateral held in the account of the counterparty at the broker or dealer if: (*a*) The independent third-party custodian is a bank as defined in Section 3(a)(6) of the Act that is not affiliated with the counterparty; (*b*) The broker or dealer, the independent third-party custodian, and the counterparty that delivered the collateral to the custodian have executed an account control agreement governing the terms under which the custodian holds and releases collateral pledged by the counterparty as initial margin that provides the broker or dealer with the same control over the collateral as would be the case if the broker or dealer controlled the collateral directly; and (*c*) The broker or dealer obtains a written opinion from outside counsel that the account control agreement is legally valid, binding, and enforceable in all material respects, including in the event of bankruptcy, insolvency, or a similar proceeding.

Similarly, the potential modifications to paragraph (c)(1)(ix) of Rule 18a–1 would provide the following deductions from net worth in lieu of collecting collateral for security-based swap and swap transactions: (*1*) *Security-based swaps.* Deducting the amounts calculated pursuant to § 240.18a–3(c)(1)(i)(B) for the account of a counterparty at the security-based swap dealer that is subject to an initial margin exception set forth in § 240.18a–3(c)(1)(iii), less the margin value of collateral held in the account of the counterparty at the security-based swap dealer. (*2*) *Swaps.* Deducting the initial margin calculated pursuant to § 240.18a–3(d)(2) for swaps other than equity swaps, or § 240.18a–1b, as applicable, in the account of a counterparty at the security-based swap dealer, less the margin value of collateral held in the account of the counterparty at the security-based swap dealer. (*3*) *Treatment of collateral held at a third-party custodian.* For the purposes of the deductions required pursuant to paragraphs (c)(1)(ix)(B)(*1*) and (*2*) of this section, collateral held by an independent third-party custodian as initial margin pursuant to Section 3E(f) of the Act or Section 4s(l) of the Commodity Exchange Act may be treated as collateral held in the account of the counterparty at the security-based swap dealer if: (*a*) The independent third-party custodian is a bank as defined in Section 3(a)(6) of the Act that is not affiliated with the counterparty; (*b*) The security-based swap dealer, the independent third-party custodian, and the counterparty that delivered the collateral to the custodian have executed an account control agreement governing the terms under which the custodian holds and releases collateral pledged by the counterparty as initial margin that provides the security-based swap dealer with the same control over the collateral as would be the case if the security-based swap dealer controlled the collateral directly; and (*c*) The security-based swap dealer obtains a written opinion from outside counsel that the account control agreement is legally valid, binding, and enforceable in all material respects, including in the event of bankruptcy, insolvency, or a similar proceeding.

5. The *2012 Proposals* noted that a nonbank SBSD would need to deduct from net worth the value of initial margin delivered to a counterparty when computing net capital.[36] A comment letter[37] encouraged the Commission to provide a means for nonbank SBSDs to post initial margin to SBSDs and other types of counterparties without incurring the capital charge. If the Commission adopts capital and margin rules applicable to SBSDs, should the Commission provide a means for a nonbank SBSD to avoid this deduction if the following conditions are met: (1) The initial margin requirement is funded by a fully executed written loan agreement with an affiliate of the broker-dealer; (2) the loan agreement provides that the lender waives re-payment of the loan until the initial margin is returned to the broker-dealer; and (3) the broker-dealer's liability to the lender can be fully satisfied by delivering the collateral serving as initial margin to the lender?[38] A Commission action providing this relief would be styled after the Staff Letter. Would this approach provide a practical solution with respect to avoiding this capital charge? If not, please explain why. Should the Commission by rule permit this approach? Are there alternatives that would more effectively and efficiently achieve this objective? If so, what are they?

Margin

6. The *2012 Proposals* included a provision that would require a nonbank SBSD to calculate a daily initial margin amount for each counterparty.[39] The nonbank SBSD could use the standardized or model-based deductions

[36] *See 2012 Proposals,* 77 FR at 70267.

[37] *See* Letter from Institute of International Bankers and Securities Industry and Financial Markets Association (June 21, 2018).

[38] In this regard, although not binding, the staff of the Division of Trading and Markets issued a no-action letter (in the context of margin collateral posted by a broker-dealer to a swap dealer or other counterparty for a non-cleared swap) that stated that the staff would not recommend enforcement action to the Commission if a broker-dealer did not take this deduction but met certain conditions. The conditions include that: (1) The initial margin requirement is funded by a fully executed written loan agreement with an affiliate of the broker-dealer; (2) the loan agreement provides that the lender waives re-payment of the loan until the initial margin is returned to the broker-dealer; and (3) the broker-dealer's liability to the lender can be fully satisfied by delivering the collateral serving as initial margin to the lender. *See* Letter from Michael A. Macchiaroli, Associate Director, Division of Trading and Markets, Commission, to Kris Dailey, Vice President, Risk Oversight and Regulation, FINRA (Aug. 19, 2016) (''Staff Letter'').

[39] *See 2012 Proposals,* 77 FR at 70261.

prescribed in the proposed capital rule for nonbank SBSDs to calculate the initial margin amount, except that initial margin for equity security-based swaps would need to be determined exclusively using the standardized deductions.

Some commenters argued that the Commission should approve a uniform initial margin model because it would reduce counterparty disputes and increase efficiency.[40] Since the publication of the *2012 Proposals,* the prudential regulators and the CFTC adopted final margin rules that permit the use of a model to calculate initial margin subject to the approval of the CFTC or a firm's prudential regulator.[41] The Commission understands that the firms subject to these final rules have widely adopted the use of an industry-developed uniform model to compute initial margin.[42] In light of the comments and the goals of this provision, the Commission requests comment on whether the margin rule should permit nonbank SBSDs to apply to use models other than proprietary capital models to compute initial margin, including applying to use a standard industry model. The purpose would be to provide flexibility to nonbank SBSDs to apply to the Commission for authorization to use a proprietary or other model to compute initial margin, and, with respect to an industry standard model, to increase transparency and decrease margin disputes among counterparties.

Would rule language as described below effect this potential modification to the rule text in the *2012 Proposals*? If not, please explain why and suggest alternative rule language. If the Commission were to use the language described below, would it strike an appropriate balance in terms of achieving the objectives of the proposed rule and addressing commenters' requests for more flexibility? If not, please explain why and suggest alternative rule language that could more effectively and efficiently strike the balance and achieve the objective.

The potential modifications to paragraph (d)(2)(i) of Rule 18a–3 would provide: For security-based swaps other than equity security-based swaps, a security-based swap dealer may apply to the Commission for authorization to use a model to compute the margin amount required by paragraph (c)(1)(i)(B) of this section and to compute the deductions required by paragraph § 240.15c3–1(c)(2)(xv) or § 240.18a–1(c)(1)(ix), as applicable, subject to the application process in § 240.15c3–1e or § 240.18a–1(d), as applicable. The model must use a ninety-nine percent (99%), one-tailed confidence level with price changes equivalent to a ten business-day movement in rates and prices, and must use risk factors sufficient to cover all the material price risks inherent in the positions for which the margin amount or deductions are being calculated, including foreign exchange or interest rate risk, credit risk, equity risk, and commodity risk, as appropriate. Empirical correlations may be recognized by the model within each broad risk category, but not across broad risk categories.

7. The *2012 Proposals* included a requirement that a nonbank SBSD would need to collect initial and variation margin from each counterparty unless an exception applies.[43] The proposed rule contained four exceptions under which variation and/or initial margin need not be collected: (1) When the counterparty is a commercial end user; (2) when the counterparty is another SBSD; (3) when the counterparty requires segregation pursuant to Section 3E(f) of the Act; and (4) when the counterparty's account holds only legacy transactions.[44]

Some commenters encouraged the Commission to adopt a threshold below which initial margin need not be collected and noted that the prudential regulators and the CFTC established a $50 million threshold (consistent with the recommendation of an international standard setting body).[45] In light of the comments and the goals of this provision, the Commission requests comment on whether it would be appropriate to establish a risk-based threshold. A fixed-dollar threshold, depending on the size and activities of the nonbank SBSD, could either be too large and, therefore, not adequately address the risk, or too small and, therefore, overcompensate for the risk. Should a risk-based threshold take into account the financial condition of the SBSD and the counterparty by providing that initial margin need not be collected from a counterparty when the amount is less than one percent (1%) or some other percent of a nonbank SBSD's tentative net capital[46] and is less than ten percent (10%) or some other percent[47] of the counterparty's net worth (in which case, only the amount above the threshold would need to be collected)? The purpose of these financial metrics would be to establish a threshold that is scalable and has a more direct relation to the risk to the nonbank SBSD arising from its security-based swap activities.

Would rule language as described below effect this potential modification to the rule text in the *2012 Proposals*? If not, please explain why and suggest alternative rule language. If the Commission were to use the language described below, would it strike an appropriate balance in terms of achieving the objectives of the proposed rule and addressing commenters' requests for a threshold? If not, please explain why and suggest alternative rule language that could more effectively and efficiently strike the balance and achieve the objective.

The potential modifications to paragraph (c)(1)(iii)(E) of Rule 18a-3 would provide that an SBSD may elect not to collect the amount required under paragraph (c)(1)(ii)(B) of this section to the extent that the amount does not exceed the lesser of: (*1*) 1 percent (1%) of the security-based swap dealer's tentative net capital; or (*2*) ten percent (10%) of the net worth of the counterparty.

8. As noted above, the *2012 Proposals* included an exception from collecting margin when the counterparty is another SBSD.[48] In particular, the Commission proposed two alternatives with respect to SBSD counterparties.[49] Under the first alternative, a nonbank SBSD would not need to collect initial margin if the counterparty is another SBSD (''Alternative A''). This approach is consistent with the broker-dealer margin rules, which generally do not require a broker-dealer to collect margin

[40] *See, e.g.,* Letter from Robert Pickel, Chief Executive Officer, International Swaps and Derivatives Association (Feb. 5, 2014) (''*ISDA 2/5/2014 Letter*'').

[41] *See Margin and Capital Requirements for Covered Swap Entities,* 80 FR 74840*; Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants,* 81 FR 636.

[42] *See, e.g.,* ISDA, *ISDA SIMM™ Deployed Today; New Industry Standard for Calculating Initial Margin Widely Adopted by Market Participants* (Sept. 1, 2016), *available at: https://www.isda.org/2016/09/01/isda-simm-deployed-today-new-industry-standard-for-calculating-initial-margin-widely-adopted-by-market-participants/.*

[43] *See 2012 Proposals,* 77 FR at 70263–69.

[44] *See id.*

[45] *See, e.g.,* Letter from Karrie McMillan, General Counsel, Investment Company Institute (Feb. 4, 2013). *See also* BCBS, IOSCO, *Margin Requirements for Non-centrally Cleared Derivatives* (Mar. 2015), *available at: http://www.bis.org/bcbs/publ/d317.pdf.*

[46] *See, e.g.,* 17 CFR 240.15c3–3a, Note E(5) (using a twenty-five percent (25%) of tentative net capital threshold for when a broker-dealer must reduce debits in the customer reserve formula).

[47] *See, e.g.,* 17 CFR 240.15c3–1(c)(2)(vi)(M)(*1*) (using a ten percent (10%) of tentative net capital threshold for the calculation of undue concentration charges).

[48] *See 2012 Proposals,* 77 FR at 70267–68.

[49] *See id.*

from another broker-dealer.[50] Under the proposed second alternative, a nonbank SBSD would be required to collect initial margin from another SBSD and the initial margin would need to be segregated pursuant to Section 3E(f) of the Act (''Alternative B'').[51]

A commenter argued that Alternative A was the preferred approach because requiring SBSDs to collect initial margin from other SBSDs would curtail the use of non-cleared security-based swaps for hedging, which would disrupt key financial services, such as those that facilitate the availability of home loans and corporate finance.[52] This commenter also argued that the requirement to collect initial margin from another SBSD would have detrimental pro-cyclical effects because it would increase collateral demands in times of market stress.[53] Other commenters supported Alternative B stating that Alternative A would permit an inappropriate build-up of systemic risk for transactions within the financial system.[54]

a. The Commission requests comment and supporting data that would assist in the quantification of the economic impacts of Alternatives A and B. The *2012 Proposals* discussed the potential for increased use of leverage, the potential for a nonbank SBSD to fail, and the potential that a default by a nonbank SBSD could translate to defaults of counterparty SBSDs.[55] The *2012 Proposals* also noted that the likelihood of these potential events occurring would be smaller under Alternative B than under Alternative A.[56] Would the proposed capital requirements complement Alternative A to reduce the potential for increased use of leverage, the potential for a nonbank SBSD to fail, and the potential that a default by a nonbank SBSD could translate to a default of counterparty SBSDs caused by exposure to credit risk in inter-dealer positions? Would there be situations where the proposed capital requirements and Alternative A would not prevent a failure of a nonbank SBSD caused by security-based swap trading losses? Would there be situations where the proposed capital requirements and Alternative A would avoid a failure of a nonbank SBSD by not imposing pro-cyclical collateral demands?

The *2012 Proposals* also noted that in comparison to Alternative A or current practices, Alternative B could have a more significant negative impact on the liquidity of nonbank SBSDs and their ability to trade in security-based swaps.[57] If Alternative B is adopted, how much initial margin would be segregated at third-party custodians and how would it impact the liquidity of nonbank SBSDs? If Alternative B is adopted, would the proposed margin requirements limit the ability of nonbank SBSDs to trade in security-based swaps?

Finally, the *2012 Proposals* noted that depending on whether Alternative A or B is adopted, the proposed margin requirements may create the potential for regulatory arbitrage.[58] In particular, the *2012 Proposals* noted that if the Commission does not require nonbank SBSDs to collect initial margin in their inter-dealer transactions (as proposed in Alternative A), while the prudential regulators require the collection of initial margin for the same transactions, intermediaries could have an incentive to conduct business through nonbank entities.[59] Would Alternative A create more opportunities for regulatory arbitrage than Alternative B, and would these regulatory arbitrage opportunities have a significant economic impact? If so, please explain how. In addition, Alternative A would differ in some respects from an international policy framework establishing recommended minimum standards for margin requirements for non-centrally cleared derivatives.[60] Would these or other differences create opportunities for regulatory arbitrage, impede transactions with other market participants, or have an impact on substituted compliance determinations?

b. If Alternative A is adopted, should the exception apply to a broader class of entities than just other SBSDs? Should it apply if the nonbank SBSD's counterparty is an SBSD, broker-dealer, bank, futures commission merchant, foreign bank, or foreign dealer? The purpose of adopting Alternative A with a modification to apply the exception to a broader class of counterparties would be to promote the liquidity of nonbank SBSDs and other market participants by reducing the amount of capital they must post as initial margin to counterparties.

Would rule language as described below effect Alternative A with the potential modification to expand the range of entities from which initial margin need not be collected? If not, please explain why and suggest alternative rule language. If the Commission were to use the language described below, would it strike an appropriate balance in terms of promoting the liquidity of nonbank SBSDs and other market participants and addressing commenters' concerns about building up systemic risk? If not, please explain why and suggest alternative rule language that could more effectively and efficiently strike the balance and achieve the objective.

The potential modifications to paragraph (c)(1)(iii)(B) of Rule 18a–3 would provide that the requirements of paragraph (c)(1)(ii)(B) of this section do not apply to an account of a counterparty that is a security-based swap dealer, swap dealer, broker or dealer, futures commission merchant, bank, foreign bank, or a foreign broker or dealer.

9. In response to the *2012 Proposals,* commenters argued that the requirements adopted pursuant to Title VII of the Dodd-Frank Act should permit the portfolio margining of security-based swaps, swaps, and related positions.[61] Portfolio margining of security-based swaps, swaps, and related positions can offer benefits to investors and the markets, including aligning margin requirements more closely with the overall risks of a customer's portfolio. Further, portfolio margining may help to improve cash flows and liquidity, and reduce volatility.

a. The Commission requests comment on whether swaps should be permitted to be held in a security-based swap account at an entity that is registered as a broker-dealer, nonbank SBSD, and swap dealer to provide a means to portfolio margin security-based swaps with swaps and related cash market and listed options positions. The Commission also requests comment on whether security-based swaps should be permitted to be held in a swap account at an entity that is registered as an FCM, swap dealer, and nonbank SBSD to provide a means to portfolio margin security-based swaps with swaps and related futures positions.

b. The Commission requests comment on whether swaps should be permitted to be held in a security-based swap

[50] *See id.*

[51] *See id.*

[52] *See* Letter from Robert Pickel, Chief Executive Officer, International Swaps and Derivatives Association (Jan. 23, 2013) (''*ISDA 1/23/2013 Letter*'').

[53] *See id.*

[54] *See, e.g.,* Letter from Americans for Financial Reform (Feb. 22, 2013).

[55] *See 2012 Proposals,* 77 FR at 70267, 70322.

[56] *See id.*

[57] *See id.* at 70322.

[58] *See id.* at 70305–06.

[59] *See id.*

[60] *See* BCBS, IOSCO, *Margin Requirements for Non-centrally Cleared Derivatives* (Mar. 2015).

[61] *See, e.g.,* Letter from Adam Jacobs, Director of Markets Regulation, Alternative Investment Management Association (Feb. 22, 2013) (''*AIMA 2/22/2013 Letter*'').

account at an entity that is registered as a nonbank SBSD and swap dealer (but not as a broker-dealer or FCM) to provide a means to portfolio margin security-based swaps and swaps in a security-based swap account. The Commission also requests comment on whether security-based swaps should be permitted to be held in a swap account at an entity that is registered as a swap dealer and SBSD (but not as an FCM or broker-dealer) to provide a means to portfolio margin security-based swaps and swaps in a swap account. If so, should such portfolio margining be subject to conditions similar to those set forth in the Commission's exemptive order permitting portfolio margining of credit default swaps (*e.g.,* conditions regarding subordination agreements and disclosures)? [62] In either scenario identified in this paragraph, should the SBSD dually registered as a swap dealer be permitted to use a model to determine portfolio margin requirements for security-based swaps and swaps that reference equity securities, provided the accounts do not hold cash market equity and listed options positions?

c. The Commission requests comment on how security-based swaps, swaps, cash market and listed options positions, and collateral held in a security-based swap account at an entity registered as a broker-dealer, nonbank SBSD, and swap dealer would be treated in a liquidation proceeding. The Commission requests comment on how security-based swaps, swaps, futures positions, and collateral held in a swap account at an entity registered as an FCM, swap dealer, and nonbank SBSD would be treated in a liquidation proceeding. Would the treatment be different if the entity was also registered as a broker-dealer? The Commission requests comment on how swaps and security-based swaps held in a security-based swap account at an entity registered as an SBSD and swap dealer would be treated in a liquidation proceeding and how security-based swaps and swaps held in a swap account at such an entity would be treated in a liquidation proceeding.

For each of the four scenarios described above, what steps should be taken to provide protections to the accountholders? What rights (including rights under the bankruptcy laws) might accountholders have to waive? Should there be limits on the types of counterparties that would be permitted to waive these rights? Should the rule require the nonbank SBSD to provide complete and accurate disclosures about the treatment of assets in a liquidation, bankruptcy, or similar proceeding under each of the scenarios described above so that accountholders and prospective accountholders can make informed decisions about the type of portfolio margin account they want to use and about waiving any rights with respect to the account?

d. The scenarios described above include permitting: (1) An entity registered as a broker-dealer, nonbank SBSD, and swap dealer to hold swaps in a security-based swap account to provide a means to portfolio margin security-based swaps with swaps and related cash market and listed options positions; and (2) an entity that is registered as an SBSD and swap dealer (but not as an FCM or broker-dealer) to hold swaps in a security-based swap account to provide a means to portfolio margin security-based swaps and swaps in a security-based swap account and to use a model to determine portfolio margin requirements for security-based swaps and swaps that reference equity securities, provided the accounts do not hold cash market equity and listed options positions.

Would rule language as described below effect these approaches to implement portfolio margining of swaps in a security-based swap account? If not, please explain why and suggest alternative rule language. If the Commission were to use the language described below, would it strike an appropriate balance in terms of achieving the objectives of the proposed rules and addressing commenters' requests to permit portfolio margining of swaps and security-based swaps? If not, please explain why and suggest alternative rule language that could more effectively and efficiently strike the balance and achieve the objective.

The potential modifications to paragraph (a)(3) of Appendix A to Rule 15c3–1 would provide: The term *related instrument* within an option class or product group refers to futures contracts, options on futures contracts, and swaps covering the same underlying instrument. In relation to options on foreign currencies a related instrument within an option class also shall include forward contracts on the same underlying currency.

The potential modifications to paragraph (a)(4) of Appendix A to Rule 15c3–1 would also provide: The term *underlying instrument* refers to long and short positions, as appropriate, covering the same foreign currency, the same security, security future, security-based swap, or a security which is exchangeable for or convertible into the underlying security within a period of 90 days. If the exchange or conversion requires the payment of money or results in a loss upon conversion at the time when the security is deemed an underlying instrument for purposes of this Appendix A, the broker or dealer will deduct from net worth the full amount of the conversion loss. The term *underlying instrument* shall not be deemed to include securities options, futures contracts, options on futures contracts, qualified stock baskets, unlisted instruments (other than security-based swaps), or swaps.

The potential modifications to paragraph (a)(3) of Appendix A to Rule 18a–1 would provide: The term *related instrument* within an option class or product group refers to futures contracts, options on futures contracts, and swaps covering the same underlying instrument. In relation to options on foreign currencies, a related instrument within an option class also shall include forward contracts on the same underlying currency.

The potential modifications to paragraph (a)(4) of Appendix A to Rule 18a–1 would provide: The term *underlying instrument* refers to long and short positions, as appropriate, covering the same foreign currency, the same security, security future, security-based swap, or a security which is exchangeable for or convertible into the underlying security within a period of 90 days. If the exchange or conversion requires the payment of money or results in a loss upon conversion at the time when the security is deemed an underlying instrument for purposes of this Appendix A, the security-based swap dealer will deduct from net worth the full amount of the conversion loss. The term underlying instrument shall not be deemed to include securities options, futures contracts, options on futures contracts, qualified stock baskets, unlisted instruments (other than security-based swaps), or swaps.

The potential modifications to paragraph (d)(2)(ii) of Rule 18a–3 would provide: Notwithstanding paragraph (d)(2)(i) of this section, a security-based swap dealer that is not registered as a broker or dealer pursuant to Section 15(b) of the Act (15 U.S.C. 78o(b)) may apply to the Commission for authorization to use a model to compute the margin amount required by paragraph (c)(1)(i)(B) of this section and to compute the deductions required by paragraph § 240.18a–1(c)(1)(ix) for equity security-based swaps and equity swaps, subject to the application process and model requirements of

[62] *See Order Granting Conditional Exemptions Under the Securities Exchange Act of 1934 in Connection with Portfolio Margining of Swaps and Security-Based Swaps,* Exchange Act Release No. 68433 (Dec. 14, 2012), 77 FR 75211 (Dec. 19, 2012).

paragraph (d)(2)(i) of this section; provided, however, the account of the counterparty subject to the requirements of this paragraph may not hold equity securities or listed options.

Segregation

10. Section 3E(f) of the Act provides that a counterparty to a non-cleared security-based swap with an SBSD can require that initial margin be segregated at a third-party custodian or waive segregation.[63] The *2012 Proposals* included a third alternative under which the initial margin for the non-cleared security-based swap could be held by the SBSD and subject to requirements modeled on the broker-dealer customer protection rule but tailored to security-based swaps (''omnibus segregation requirements'').[64] The omnibus segregation requirements would be mandatory for initial margin held by the SBSD for cleared security-based swaps.

a. The Commission received a number of comments asking technical questions about how the proposed omnibus segregation requirements would operate in the context of security-based swap transactions, including specific questions about the computation of the reserve formula, and what types of hedging would be permitted under the proposed definition of ''excess securities collateral.''[65] The Commission requests comment on whether there are aspects of the proposed omnibus segregation requirements where greater clarity regarding the application of the rule would be helpful. If so, please identify them and suggest appropriate modifications to the proposed rule.

b. The *2013 Proposals* would treat segregation as a transaction-level requirement, and the Commission proposed paragraph (e) of Rule 18a–4 to prescribe the scope of application of the segregation requirements in Section 3E(f) of the Act and Rule 18a–4.[66] The proposed cross-border application of these segregation requirements to a foreign SBSD or foreign MSBSP depended on whether it is a registered broker-dealer, a U.S. branch or agency of a foreign bank, or neither of the above, and whether the security-based swaps are cleared or non-cleared.[67] The Commission requests comment on whether there are aspects of the proposed cross-border application of the segregation requirements where greater clarity regarding the application of the rule would be helpful. If so, please identify them and suggest appropriate modifications to the proposed rule.

c. The *2013 Proposals* provided that a foreign SBSD that is a U.S. branch or agency of a foreign bank must comply with segregation requirements with respect to security-based swap transactions with U.S. security-based swap customers, but not with foreign security-based swap customers.[68] Should the segregation requirements apply to certain foreign security-based swap customers? In particular, the Commission requests comment on whether a foreign SBSD that is not a broker-dealer and is a foreign bank should be required to comply with the segregation requirements (1) with respect to U.S. security-based swap customers (regardless of which branch or agency the customer's transactions arise out of), and (2) with respect to a foreign security-based swap customer if the foreign SBSD holds funds or other property arising out of a transaction had by such person with a U.S. branch or agency of the foreign SBSD.

11. The Commission received a comment that the broker-dealer customer protection rule (Rule 15c3–3) should be amended to take into account margin that is posted at a clearing agency by broker-dealers not registered as SBSDs.[69] The Commission requests comment on whether Rule 15c3–3 should be amended to add a new paragraph (p) and a new Exhibit B that would contain segregation requirements and a customer reserve formula that parallel those in proposed Rule 18a–4. The security-based swap segregation requirements that would be added to Rule 15c3–3 would be substantially the same as the requirements in each paragraph of proposed Rule 18a–4.[70] The purpose would be to permit broker-dealers that are not registered as SBSDs but that engage in security-based swap activities to use segregation requirements that parallel those in proposed Rule 18a–4 and which are tailored to security-based swaps. In addition, the purpose would be to locate in Rule 15c3–3 the security-based swap segregation requirements for entities registered as a broker-dealer and SBSD. Proposed Rule 18a–4 would apply to SBSDs that are not registered as broker-dealers.

12. The *2012 Proposals* include a definition of ''excess securities collateral'' to identify securities and money market instruments received from security-based swap customers that must be held in physical possession or control.[71] In particular, securities and money market instruments that are not being used to collateralize the SBSD's current exposure to the customer (*i.e.,* exceed the variation margin requirement) would need to be in the physical possession or control of the SBSD unless one of two exceptions applied.[72] The exceptions are that the securities and money market instruments are held in a: (1) Qualified clearing agency account but only to the extent they are being used to meet a margin requirement of the clearing agency; or (2) qualified SBSD account but only to the extent they are being used to meet a margin requirement that applies to the other SBSD resulting from entering into a non-cleared security-based swap transaction with the other SBSD to offset the risk of a non-cleared security-based swap transaction between the SBSD and the customer.[73] In addition, the *2012 Proposals* included a requirement for an SBSD to perform a customer reserve formula calculation.[74] Under the proposal, an SBSD could include as a debit item in the formula cash collateral posted to a clearing agency or another SBSD under the same circumstances as the exceptions to the definition of ''excess securities collateral.''[75] The prudential regulators require initial margin posted by an SBSD to a bank SBSD to be held at a third-party custodian (rather than being held directly by the bank SBSD).[76] This means that if an SBSD enters into a transaction with a bank SBSD to hedge a non-cleared security-based swap transaction with a security-based swap customer, the SBSD may have to post initial margin to the bank SBSD and that initial margin would need to be held by a third-party custodian rather than directly by the bank SBSD.

The Commission requests comment on how initial margin posted by an SBSD to a bank SBSD to hedge a transaction with a security-based swap customer should be treated for purposes of the possession or control and customer reserve requirements in the

[63] *See* 15 U.S.C. 78c–5(f)(3).

[64] *See 2012 Proposals,* 77 FR at 70274–88; 17 CFR 240.15c3–3.

[65] *See, e.g., SIFMA 2/22/2013 Letter.*

[66] *See 2013 Proposals,* 78 FR at 31010–11, 31018–22, 31209–10.

[67] *See id.* at 31018–22.

[68] *See id.*

[69] *See* Letter from Kathleen M. Cronin, CME Group Inc. (Feb. 22, 2013).

[70] The provisions of paragraph (d) of proposed Rule 18a–4 would not apply to a broker-dealer that is not also registered as either an SBSD or MSBSP because Section 3E(f)(1)(A) of the Act does not apply to broker-dealers. *See 2012 Proposals,* 77 FR at 70287.

[71] *See 2012 Proposals,* 77 FR at 70278–70282.

[72] *See id.*

[73] *See id.*

[74] *See id.* at 70282–87.

[75] *See id.*

[76] *See* 12 CFR 45.7; 12 CFR 237.7; 12 CFR 624.7; 12 CFR 1221.7; 12 CFR 349.7.

proposed SBSD segregation rule. For purposes of the possession or control and customer reserve account requirements, should the initial margin be treated similarly to how initial margin an SBSD posts to a nonbank SBSD is treated if the purpose is to enter into a transaction that hedges a transaction with a security-based swap customer? The purpose would be to accommodate an SBSD that elects to enter into a hedging transaction with a bank SBSD and must post initial margin that is segregated at a third-party custodian.

Would rule language as described below effect this potential modification to the rule text in the *2012 Proposals*? If not, please explain why and suggest alternative rule language. If the Commission were to use the language described below, would it strike an appropriate balance in terms of achieving the objectives of the proposed rule and accommodating SBSDs that elect to hedge a non-cleared security-based swap transaction by entering into an off-setting transaction with a bank SBSD? If not, please explain why and suggest alternative rule language that could more effectively and efficiently strike the balance and achieve the objective.

The potential modifications to paragraph (p)(1)(ii) of Rule 15c3–3 would provide: The term *excess securities collateral* means securities and money market instruments carried for the account of a security-based swap customer that have a market value in excess of the current exposure of the broker or dealer (after reducing the current exposure by the amount of cash in the account) to the security-based swap customer, excluding: (A) Securities and money market instruments held in a qualified clearing agency account but only to the extent the securities and money market instruments are being used to meet a margin requirement of the clearing agency resulting from a security-based swap transaction of the security-based swap customer; and (B) securities and money market instruments held in a qualified registered security-based swap dealer account or in a third-party custodial account but only to the extent the securities and money market instruments are being used to meet a regulatory margin requirement of a security-based swap dealer resulting from the broker or dealer entering into a non-cleared security-based swap transaction with the security-based swap dealer to offset the risk of a non-cleared security-based swap transaction between the broker or dealer and the security-based swap customer.

The potential modifications to paragraph (p)(1)(viii) of Rule 15c3–3 would provide: The term *third-party custodial account* means an account carried by an independent third-party custodian that meets the following conditions: (A) The account is established for the purposes of meeting regulatory margin requirements of another security-based swap dealer; (B) The account is carried by a bank; (C) The account is designated for and on behalf of the broker or dealer for the benefit of its security-based swap customers and the account is subject to a written acknowledgement by the bank provided to and retained by the broker or dealer that the funds and other property held in the account are being held by the bank for the exclusive benefit of the security-based swap customers of the broker or dealer and are being kept separate from any other accounts maintained by the broker or dealer with the bank; and (D) The account is subject to a written contract between the broker or dealer and the bank which provides that the funds and other property in the account shall at no time be used directly or indirectly as security for a loan or other extension of credit to the security-based swap dealer by the bank and, shall be subject to no right, charge, security interest, lien, or claim of any kind in favor of the bank or any person claiming through the bank.

The potential modifications to Line 16 of Exhibit B to Rule 15c3–3 would provide: Margin related to non-cleared security-based swap transactions in accounts carried for security-based swap customers required and held in a qualified registered security-based swap dealer account at another security-based swap dealer or at a third-party custodial account.

The potential modifications to paragraph (a)(2) of Rule 18a–4 would provide: The term *excess securities collateral* means securities and money market instruments carried for the account of a security-based swap customer that have a market value in excess of the current exposure of the security-based swap dealer (after reducing the current exposure by the amount of cash in the account) to the security-based swap customer, excluding (i) securities and money market instruments held in a qualified clearing agency account but only to the extent the securities and money market instruments are being used to meet a margin requirement of the clearing agency resulting from a security-based swap transaction of the security-based swap customer; and (ii) securities and money market instruments held in a qualified registered security-based swap dealer account or in a third-party custodial account but only to the extent the securities and money market instruments are being used to meet a regulatory margin requirement of another security-based swap dealer resulting from the security-based swap dealer entering into a non-cleared security-based swap transaction with the other security-based swap dealer to offset the risk of a non-cleared security-based swap transaction between the security-based swap dealer and the security-based swap customer.

The potential modifications to paragraph (a)(10) of Rule 18a–4 would also provide: The term *third-party custodial account* means an account carried by an independent third-party custodian that meets the following conditions: (i) The account is established for the purposes of meeting regulatory margin requirements of another security-based swap dealer; (ii) The account is carried by a bank; (iii) The account is designated for and on behalf of the security-based swap dealer for the benefit of its security-based swap customers and the account is subject to a written acknowledgement by the bank provided to and retained by the security-based swap dealer that the funds and other property held in the account are being held by the bank for the exclusive benefit of the security-based swap customers of the security-based swap dealer and are being kept separate from any other accounts maintained by the security-based swap dealer with the bank; and (iv) The account is subject to a written contract between the security-based swap dealer and the bank which provides that the funds and other property in the account shall at no time be used directly or indirectly as security for a loan or other extension of credit to the security-based swap dealer by the bank and, shall be subject to no right, charge, security interest, lien, or claim of any kind in favor of the bank or any person claiming through the bank.

The potential modifications to Line 14 of Exhibit A to Rule 18a–4 would provide: Margin related to non-cleared security-based swap transactions in accounts carried for security-based swap customers required and held in a qualified registered security-based swap dealer account at another security-based swap dealer or at a third-party custodial account.

13. The *2012 Proposals* required an SBSD to deduct the amount of funds held in a security-based swap customer reserve account at a single bank to the extent the amount exceeds ten percent (10%) of the equity capital of the bank

as reported by the bank in its most recent Consolidated Report of Condition and Income (''Call Report'').[77] This proposal was consistent with amendments to Rule 15c3–3 that at that time were still in the proposal stage.[78] In 2013, the Commission adopted with modifications the amendments to Rule 15c3–3.[79] The modifications increased the threshold applicable to broker-dealer customer reserve accounts held at a bank to fifteen percent (15%) and excluded cash on deposit at an affiliated bank.

The Commission requests comment on whether, for consistency with broker-dealers, the threshold applicable to SBSD customer reserve accounts held at a bank should be increased to fifteen percent (15%) of the bank's equity capital and whether any cash deposited with an affiliated bank should be excluded. The purpose would be to more closely align the proposed segregation requirements for security-based swaps with the existing customer reserve requirements in Rule 15c3–3, as amended in 2013. Should the fifteen percent (15%) threshold not apply if the SBSD is a bank and maintains the security-based swap customer reserve account itself rather than at an affiliated or non-affiliated bank? The purpose of this exception would be to accommodate a bank SBSD that holds the customer reserve account directly.

The changes discussed above would modify paragraph (c)(1) of proposed Rule 18a–4 and new paragraph (p)(3) of proposed Rule 15c3–3 to more closely align them with the 2013 amendments to Rule 15c3–3 and, with respect to proposed Rule 18a–4, establish an exception from the fifteen percent (15%) threshold for a bank SBSD that maintains the security-based swap customer reserve account itself. Would rule language as described below effect this potential modification to the rule text in the *2012 Proposals*? If not, please explain why and suggest alternative rule language. If the Commission were to use the language described below, would it strike an appropriate balance in terms of achieving the objectives of the proposed rule and providing sufficient flexibility to SBSDs in terms of locating their reserve account deposits? If not, please explain why and suggest alternative rule language that could more effectively and efficiently strike the balance and achieve the objective.

The potential modifications to paragraph (p)(3)(i) of Rule 15c3–3 would provide: In determining the amount maintained in a special reserve account for the exclusive benefit of security-based swap customers, the security-based swap dealer must deduct (A) the amount of cash deposited with a single non-affiliated bank to the extent the amount exceeds fifteen percent (15%) of the equity capital of the bank as reported by the bank in its most recent Call Report or any successor form the bank is required to file by its appropriate federal banking agency (as defined by Section 3 of the Federal Deposit Insurance Act (12 U.S.C. 1813)); and (B) the total amount of cash deposited with an affiliated bank.

Similarly, the potential modifications to paragraph (c)(1)(i) of Rule 18a–4 would provide: In determining the amount maintained in a special reserve account for the exclusive benefit of security-based swap customers, the security-based swap dealer must deduct (A) the amount of cash deposited with a single non-affiliated bank to the extent the amount exceeds fifteen percent (15%) of the equity capital of the bank as reported by the bank in its most recent Call Report or any successor form the bank is required to file by its appropriate federal banking agency (as defined by Section 3 of the Federal Deposit Insurance Act (12 U.S.C. 1813)); and (B) for a security-based swap dealer for which there is not a prudential regulator, the total amount of cash deposited with an affiliated bank.

The potential modifications to paragraph (c)(1)(ii) of Rule 18a–4 would provide the following exception: A security-based swap dealer for which there is a prudential regulator need not take the deduction specified in paragraph (c)(1)(i)(D) of this section if it maintains the special reserve account for the exclusive benefit of security-based swap customers itself rather than at an affiliated or non-affiliated bank.

Substituted Compliance

14. The *2013 Proposals* would make substituted compliance with respect to capital and margin requirements available to foreign nonbank SBSDs that are not also registered as broker-dealers.[80] Upon a Commission substituted compliance determination, this type of SBSD would be able to satisfy relevant capital and margin requirements by complying with corresponding requirements under a foreign regulatory system. The Commission requests comment on whether the potential modifications to the rule text in the *2012 Proposals* discussed in this release would have an impact on substituted compliance determinations. If so, please explain how.

A number of commenters requested that the Commission consider consistency with the prudential regulators, international standards, and foreign regulators when making substituted compliance determinations with respect to the proposed nonbank SBSD capital requirements.[81]

a. Commenters generally requested additional guidance regarding the criteria the Commission would consider when making substituted compliance determinations.[82] In light of the comments and the goals of this provision, the Commission requests comment on the factors it should consider in making a substituted compliance determination with respect to the proposed nonbank SBSD capital requirements of Section 15F(e) of the Act and proposed Rule 18a–1. In making a substituted compliance determination, should the Commission consider whether the capital requirements of the foreign financial regulatory system are designed to help ensure the safety and soundness of registrants in a manner that is comparable to the proposed capital requirements for nonbank SBSDs?[83] In addition, the proposed nonbank SBSD capital rule prescribes a net liquid assets test that requires the firm to have an amount of highly liquid assets that exceeds the amount of the firm's unsubordinated liabilities.[84] In terms of the conditions that might be included in an order making an affirmative substituted compliance determination, should the Commission consider a condition that requires foreign nonbank SBSDs relying on the order to maintain liquid assets in excess of their unsubordinated liabilities?[85] Are there

[77] *See 2012 Proposals,* 77 FR at 70282–86.

[78] *See Amendments to Financial Responsibility Rules for Broker-Dealers,* Exchange Act Release No. 55431 (Mar. 9, 2007), 72 FR 12862 (Mar. 19, 2007).

[79] *See Financial Responsibility Rules for Broker-Dealers,* Exchange Act Release No. 70072 (Jul. 30, 2013), 78 FR 51824, 51832–35 (Aug. 21, 2013).

[80] *See 2013 Proposals,* 78 FR at 31207–08.

[81] *See, e.g., ISDA 1/23/2013 Letter.*

[82] *See, e.g.,* Letter from the Coalition for Derivatives End-Users (Agricultural Retailers Association, Business Roundtable, Financial Executives International, National Association of Corporate Treasurers, National Association of Manufacturers, U.S. Chamber of Commerce) (Aug. 21, 2013).

[83] *See, e.g.,* 15 U.S.C. 78o–10(e)(3)(A).

[84] *See 2012 Proposals,* 77 FR at 70221–25.

[85] *See Interpretation Guide to Net Capital Computation for Brokers and Dealers,* Exchange Act Release No. 8024 (Jan. 18, 1967), 32 FR 856 (Jan. 25, 1967) (''Rule 15c3–1 (17 CFR 240.15c3–1) was adopted to provide safeguards for public investors by setting standards of financial responsibility to be met by brokers and dealers. The basic concept of the rule is liquidity; its object being to require a broker-dealer to have at all times sufficient liquid assets to cover his current indebtedness.'') (footnotes omitted); *Net Capital Requirements for Brokers and Dealers,* Exchange Act Release No. 15426 (Dec. 21, 1978), 44 FR 1754 (Jan. 8, 1979)

reasonable alternatives to a net liquid assets test that could be the basis for a condition that is designed to ensure the foreign nonbank SBSD maintains sufficient liquidity to meet its obligations to security-based swap customers and other creditors? If so, describe them and explain how they would achieve this objective. Would these alternatives be appropriate for a domestic nonbank SBSD that is not registered as a broker-dealer? If so, explain why. Should the Commission consider a condition that the foreign nonbank SBSD not have a disproportionate number of U.S. customers? If not, explain why.

b. The Commission requests comment on the composition of the balance sheets of entities in foreign jurisdictions that may register as nonbank SBSDs. Are the assets and liabilities of these foreign entities similar to the assets and liabilities of U.S. broker-dealers that are subject to the net liquid assets test? If not, explain the differences.

c. The approach described in 14.a would modify Rule 3a71–6 (proposed as Exchange Act Rule 3a71–5 at 78 FR 30967, 31207–08) to describe factors that the Commission would consider in making a substituted compliance determination with respect to the proposed nonbank SBSD capital requirements.[86] Would rule language as described below effect this potential modification to the rule text in the *2012 Proposals*? If not, please explain why and suggest alternative rule language. If the Commission were to use the language described below, would it strike an appropriate balance in terms of achieving the objectives of the proposed rule and addressing the commenters' concerns described above? If not, please explain why and suggest alternative rule language that could more effectively and efficiently strike the balance and achieve the objective.

The potential modifications to paragraph (d)(4) of Rule 3a71–6 would provide that substituted compliance is available with respect to: The capital requirements of Section 15F(e) of the Act (15 U.S.C. 78o–10(e)) and § 240.18a–1; provided, however, that prior to making such substituted compliance determination with respect to security-based swap dealers, the Commission intends to consider (in addition to any conditions imposed) whether the capital requirements of the foreign financial regulatory system are designed to help ensure the safety and soundness of registrants in a manner that is comparable to the applicable provisions arising under the Act and its rules and regulations.

Compliance Date

15. In the Commission's release establishing the registration process for SBSDs and MSBSPs, the Commission provided that the compliance date for the SBSD and MSBSP registration requirements will be the later of: Six months after the date of publication in the **Federal Register** of final rules establishing capital, margin, and segregation requirements for SBSDs and MSBSPs; the compliance date of final rules establishing recordkeeping and reporting requirements for SBSDs and MSBSPs; the compliance date of final rules establishing business conduct requirements under Sections 15F(h) and 15F(k) of the Exchange Act; or the compliance date for final rules establishing a process for a registered SBSD or MSBSP to make an application to the Commission to allow an associated person who is subject to a statutory disqualification to effect or be involved in effecting security-based swaps on the SBSD or MSBSP's behalf (the ''Registration Compliance Date'').[87] Would this provide enough time for registrants to take the necessary steps to come into compliance with applicable requirements? If not, explain why. Would a longer period, such as 18 months after the date of publication of the last of four releases noted above in the **Federal Register**, be more appropriate? If so, explain why. Would a shorter period be more appropriate? If so, explain why. Should the Commission consider the timing of the phased implementation of initial margin requirements provided for by other regulators in making any changes to the compliance period?[88] If so, explain why.

Additional Requests for Comment—Economic Implications

16. The *Proposals* contain economic analyses seeking to identify and consider the benefits and costs—including the effects on efficiency, competition and capital formation—that would result from the proposed capital, margin, and segregation requirements. To assist in the quantification of the economic effects of the proposed requirements, the Commission requests comment and supporting data on the current risk management practices that support the trading activity in security-based swaps. Specifically, what are the main sources of funding available to entities that would be registering as nonbank SBSDs to support their trading activity? How much of the capital available to an entity that would be registering as a nonbank SBSD consists of liquid capital? What are typical risk management procedures for dealing with losses stemming from the market risk of security-based swap positions? What are typical risk management procedures for dealing with losses stemming from the credit risk of uncollateralized security-based swap positions? In the event that losses from trading activities overcome the available liquid capital, how are excess losses dealt with? What are the operational risks and concerns associated with maintaining adequate levels of capital?

The Commission also requests comment and data on how the baseline of the economic analyses has changed since the publication of the *Proposals.* For example, in 2015, the U.S. prudential regulators and the CFTC adopted final rules on minimum margin requirements for non-cleared swaps that began to be implemented in September 2016. A June 2017 survey on dealer financing terms noted that some of the survey respondents indicated that their clients' transaction volume or their own transaction volume in non-cleared swaps decreased somewhat over the period of September 2016 to June 2017.[89] However, the respondents reported no changes in the prices that

(''The rule requires brokers or dealers to have sufficient cash or liquid assets to protect the cash or securities positions carried in their customers' accounts. The thrust of the rule is to insure that a broker or dealer has sufficient liquid assets to cover current indebtedness.''); *Net Capital Requirements for Brokers and Dealers,* Exchange Act Release No. 26402 (Dec. 28, 1989), 54 FR 315 (Jan. 5, 1989) (''The rule's design is that broker-dealers maintain liquid assets in sufficient amounts to enable them to satisfy promptly their liabilities. The rule accomplishes this by requiring broker-dealers to maintain liquid assets in excess of their liabilities to protect against potential market and credit risks.'') (footnote omitted). *See also Cross-Border Security-Based Swap Activities; Re-Proposal of Regulation SBSR and Certain Rules and Forms Relating to the Registration of Security-Based Swap Dealers and Major Security-Based Swap Participants; Proposed Rule,* 78 FR at 31090.

[86] *See* 17 CFR 240.3a71–6.

[87] *See Registration Process for Security-Based Swap Dealers and Major Security-Based Swap Participants,* Exchange Act Release No. 75611 (Aug. 5, 2015), 80 FR 48963 (Aug. 14, 2015).

[88] *See Margin and Capital Requirements for Covered Swap Entities,* 80 FR at 74849–51 (adopting compliance dates phasing-in initial margin requirements beginning September 1, 2016 and ending September 1, 2020 for bank swap dealers, bank SBSDs, bank swap participants, and bank MSBSPs); *Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants,* 81 FR at 674–677 (adopting compliance dates phasing-in initial margin requirements beginning September 1, 2016 and ending September 1, 2020 for nonbank swap dealers and nonbank major swap participants).

[89] *See* Yesol Huh, Division of Research and Statistics, Board of Governors of the Federal Reserve System, *The June 2017 Senior Credit Officer Opinion Survey on Dealer Financing Terms, available at https://www.federalreserve.gov/data/scoos/files/scoos_201706.pdf.*

they quote to their clients in non-cleared swaps over this period. One-fifth of the survey respondents also reported that they would be less likely to exchange daily variation margin with mutual funds, exchange-traded funds, pension plans, endowments, and separately managed accounts established with investment advisers due primarily to lack of operational readiness (*e.g.,* the need to establish or update the necessary credit support annexes to cover daily exchange of variation margin) over this period. Two-fifths of the survey respondents also reported that the volume of mark and collateral disputes on variation margin has increased somewhat over this period. Furthermore, the survey noted that there is variation among respondents with respect to the number of days it takes to resolve a mark and collateral dispute on variation margin, with one-third reporting less than two days, while three-fifths reporting more than two days but less than a week, on average. This type of data could provide insight regarding how entities that may register as nonbank SBSDs may respond to the Commission's final margin requirements.

Commenters are asked to describe changes, if applicable, in: (1) The trading volumes in the relevant security-based swap and swap markets; (2) the regulatory structure of these markets; and (3) the number and types of entities that participate in these markets. Commenters also are asked to describe how those changes in the baseline would impact the potential benefits and costs—including the effects on efficiency, competition and capital formation—of the *Proposals* as well as the potential benefits and costs—including the effects on efficiency, competition and capital formation—that would result from the potential alternatives described in the questions above taking the changes in the baseline into account (if applicable).

Finally, the Commission requests comment on whether there are economic considerations apart from those discussed in the *Proposals* that should be considered in the economic analysis of the capital, margin, and segregation requirements as well as the alternatives described in the questions above.

By the Commission.

Dated: October 11, 2018.

Eduardo A. Aleman,

Assistant Secretary.

[FR Doc. 2018–22531 Filed 10–18–18; 8:45 am]

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DEPARTMENT OF DEFENSE

Office of the Secretary

32 CFR Part 151

[Docket ID: DOD–2012–OS–0069]

RIN 0790–AI89

Foreign Criminal and Civil Jurisdiction

AGENCY: Department of Defense (DoD).

ACTION: Proposed rule.

SUMMARY: This rule describes procedures concerning trial by foreign criminal courts of, treatment in foreign prisons of, and the payment of counsel fees in certain civil cases for individuals referred to collectively in this rule as ''dependents of DoD personnel.''

DATES: Comments must be received by December 18, 2018.

ADDRESSES: You may submit comments, identified by docket number and or RIN number and title, by any of the following methods:

- *Federal Rulemaking Portal: http://www.regulations.gov.* Follow the instructions for submitting comments.
- *Mail:* Department of Defense, Office of the Chief Management Officer, Directorate for Oversight and Compliance, 4800 Mark Center Drive, Mailbox #24, Suite 08D09, Alexandria, VA 22350–1700.

Instructions: All submissions received must include the agency name and docket number or Regulatory Information Number (RIN). The general policy for comments and other submissions from members of the public is to make these submissions available at *http://www.regulations.gov* as they are received without change, including any personal identifiers or contact information.

FOR FURTHER INFORMATION CONTACT: Bart Wager, 703–571–9355.

SUPPLEMENTARY INFORMATION:

Authorities

Taken together, two statutes authorize the Secretary of Defense to issue legally binding guidelines on the Department of Defense. Under 10 U.S.C. 113, the Secretary has ''authority, direction, and control'' over the Department of Defense. The Department of Defense is an ''executive department,'' and the Secretary, as the head of an ''executive department,'' is empowered under 5 U.S.C. 301 to issue departmental regulations. The General Counsel of the Department of Defense has been delegated authority under Department of Defense Directive 5145.01, ''General Counsel of the Department of Defense'' (available at *http://www.esd.whs.mil/Portals/54/Documents/DD/issuances/dodd/514501p.pdf*), to issue this policy. Title 10 U.S.C. 1037 authorizes the payment of counsel and other fees in certain cases in foreign judicial tribunals and administrative agencies.

Revisions Proposed by This Rule

This rule will update 32 CFR part 151, ''Status of Forces Policies and Information'' which was last updated on March 28, 1980. In 1985, Section 681 of Public Law 99–145 amended 10 U.S.C. 1037 to authorize the payment of counsel fees for those ''not subject to the Uniform Code of Military Justice.'' So this rule proposes to update and describe procedures concerning trial by foreign criminal courts of, treatment in foreign prisons of, and the payment of counsel fees in certain civil cases for command-sponsored and non-command sponsored dependents of Armed Forces members, and dependents of nationals and non-nationals of the United States who are serving with or accompanying the Military Services.

Summary of the Major Provisions

For dependents of DoD personnel, when those dependents are in a foreign country as a result of accompanying DoD personnel who are assigned duty in that country—it is Department of Defense policy to (a) maximize the exercise of U.S. jurisdiction to the extent permissible under applicable status of forces agreements or other forms of jurisdiction arrangements; (b) protect, to the maximum extent possible, the rights of dependents of DoD personnel who may be subject to criminal trial by foreign courts and imprisonment in foreign prisons; and (c) secure, where possible, the release of an accused to the custody of U.S. authorities pending completion of all foreign judicial proceedings.

A ''designated commanding officer'' (DCO) in each geographical area assigned to a Combatant Command is to (1) cooperate with the appropriate U.S. Chief of Mission and to the maximum extent possible, ensure that dependents of DoD personnel receive the same treatment, rights, and support as would be extended to U.S. Armed Forces members in comparable situations; (2) report informally and immediately to the General Counsel of the Department of Defense, the applicable geographic Combatant Commander, and the General Counsel and the Judge Advocate General of the respective Military Department, or, in the case of the Marine Corps, to the General Counsel of the Navy and the Staff Judge Advocate to the Commandant of the Marine