

Clients & Friends Memo

SEC SBSD Recordkeeping and Reporting Proposal

April 23, 2014

The SEC has published proposed recordkeeping, reporting and capital deficiency notification requirements that would apply to security-based swap dealers (“**SBSDs**”) and major security-based swap participants (“**MSBSPs**”)¹ as well as to other SEC-registered broker-dealers that enter into security-based swaps.² The proposing Release contains a number of largely non-substantive, technical amendments to the existing recordkeeping and reporting requirements applicable to broker-dealers.³

Piece of Larger Rulemaking Scheme

Many of the new proposed rules and rule amendments are directly tied to previously proposed rules and rule amendments that would be applicable to SBSDs and security-based swaps. That is, the new proposals in this Release would impose recordkeeping and reporting requirements intended to document the SEC’s previously proposed prudential and conduct requirements applicable to SBSDs and security-based swaps.⁴ For example, certain of the newly proposed recordkeeping requirements are tied to the reporting requirements under Proposed Regulation SBSR.⁵ In a number of places the SEC expressly notes that the requirements proposed in the Release would be subject to change based on any changes to these earlier rules proposals as they are finalized.

Modeled Closely on Existing Rules

The SEC modeled its proposals very closely on the existing rules that apply to broker-dealers,

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- ¹ In the remainder of this memo we largely refer generically to only SBSDs without additional mention of MSBSPs. This is done for ease of reading and in light of the fact that it is unlikely that any firms will register as a MSBSPs.
 - ² SEC Release No. 34-71958 (the “**Release**”), available at <http://www.sec.gov/rules/proposed/2014/34-71958.pdf>.
 - ³ The Release also proposes to expand its proposed capital rules for SBSDs to add a capital charge, in relation to securities differences, that currently applies to ordinary broker-dealers. The SEC notes in the Release that this particular capital charge had been inadvertently omitted from its prior rule proposals for “stand-alone,” SBSDs. *i.e.*, SBSDs that are not banks or broker-dealers.
 - ⁴ See, *e.g.*, SEC Release No. 34-68071, 77 Fed. Reg. 70214 (Nov. 23, 2012) (capital and margin requirements); SEC Release No. 34-69490, 78 Fed. Reg. 30968 (May 23, 2013) (reporting requirements); SEC Release No. 34-64766, 76 Fed. Reg. 42396 (July 18, 2011) (business conduct standards).
 - ⁵ See Release at p. 24-26 & n. 91.

particularly Exchange Act Rules 17a-3 (recordkeeping), 17a-4 (record retention), 17a-5 (financial reporting), 17a-11 (notification of financial or other problems), 17a-13 (securities counts) and the FOCUS Report (form of financial report). In general, firms registered as broker-dealers would be subject to the same set of rules that they are today, with the scope of such rules expanding and becoming somewhat more detailed to reflect the scheme for regulating SBSBs and security-based swaps under Dodd-Frank. Firms that are not currently required to register as broker-dealers, but that will be required to register as SBSBs, would be subject to a new set of rules that largely parallel the rules applicable to broker-dealers.⁶ **See Appendix A for a chart that shows the existing SEC rule that is the model for the various newly proposed rules.**

Numerous Types of Registrants and Rule Sets

Although the proposed rules are not inherently complicated insofar as they are closely modeled on the existing rules, the SEC proposed eight variants of the rules, depending on factors including whether the regulated firm is a (i) broker-dealer, (ii) bank, (iii) SBSB, (iv) MSBSP, and (v) how it computes its net capital. **See Appendix B for a chart that details which specific rule requirements apply to which types of entities.**

Banks as Registrants

One of the eight sets of rules is intended to apply to banks that act as SBSBs or MSBSPs. This rule set is somewhat more limited than those that would apply to non-bank SBSBs, as the SEC recognizes that its recordkeeping and reporting requirements for banks are confined to the banks' security-based swap business given that the margin, capital and other prudential requirements for banks will be administered by the bank regulators.

The SEC proposed rules for SBSBs should also be read in light of the fact that if Section 716 of Dodd-Frank (also known as the "Lincoln Amendment" or "push-out rule") goes into effect, banks would effectively be prohibited from acting as SBSBs, and this set of rules would become moot. Thus, there may be a temptation on the part of banks not to comment on this rule set on the assumption it will never be applicable. While that would be understandable, banks should consider the possibility that Section 716 could eventually be amended, repealed or rendered ineffective,⁷ and thus there is a potential benefit to commenting on the bank SBSB rule set.⁸

⁶ For example, proposed Rule 18a-5, which sets forth the recordkeeping requirements that apply to SBSBs, closely tracks existing Rule 17a-4, which sets forth the recordkeeping requirements that currently apply to ordinary broker-dealers.

⁷ See, e.g., H.R. 992 (which passed the House in late 2013 and would substantially amend Section 716).

⁸ Section 716 is one of the most problematic provisions in Dodd-Frank and also one that will be among the most difficult to implement, as it will require market participants to renegotiate a massive number of contracts. It is difficult to see how this could be done in any reasonable length of time, given that these contracts were put in place over two decades, and because novating the contracts out of banks would not be a simple matter of assignment, given that the credit, collateral and other terms will be materially different.

Comparison to CFTC Requirements for Swap Dealers

The SEC did not address, at least not with significant detail, how these proposals compare to the requirements applicable to swap dealers under the CFTC rules.⁹ As a general matter, the SEC proposals provide a less radical, and generally more workable, approach to implementing the broad statutory requirements found in Title VII of Dodd-Frank that accord to a great extent with existing practices and regulatory requirements.

One example of the contrast in the CFTC and SEC approaches is how the SEC treats the statutory requirement to produce and maintain "recordings of telephone calls" as part of the "daily trading records" of SBSBs.¹⁰ The CFTC took an expansive view of the requirements called for by the statutory language applicable to swap dealers,¹¹ which has resulted in significant operational questions and in delays of the implementation of the rule; by contrast, the SEC specifically limits the application of its rules to the terms of the statute, requiring telephone recordings only if "required to be maintained pursuant to Section 15F(g)(1) of the [Exchange] Act." Significantly, the SEC adds that the recordings would only be required to be retained if the registrant voluntarily chooses to record.¹² Thus, for example, an SBSB would only need to keep recorded telephone conversations (if made) as part of the "daily trading records of [its] security-based swaps," but not, among other things, as part of its securities business (e.g., if it is a broker-dealer).¹³

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⁹ Though the SEC notes, in the economic analysis portion of the Release that it believes that its proposals are "broadly consistent with the approach taken by the CFTC." See Release at p. 306.

¹⁰ See Exchange Act Section 15F(g)(1).

¹¹ See CFTC Regulation 23.202 (implementing Section 4s(g) of the Commodity Exchange Act, which mirrors Section 15F(g) of the Securities Exchange Act of 1934).

¹² See Release at 244 (discussing amendments to Rule 17a-4).

¹³ This distinction is notable in part because the SEC has not previously interpreted the term "communications" to include telephonic communications under Rule 17a-4.

Appendix A

Existing Broker-Dealer Rule and Title	New Swap Dealer Rough Equivalent Rule
Exchange Act Rule 17a-3: Records to Be Made by Certain Exchange Members, Brokers and Dealers	Exchange Act Rule 18a-5
Exchange Act Rule 17a-4: Records to Be Preserved by Certain Exchange Members, Brokers and Dealers	Exchange Act Rule 18a-6
Exchange Act Rule 17a-5: Reports to Be Made by Certain Brokers and Dealers	Exchange Act Rule 18a-7
FOCUS Report	Form SBS
Exchange Act Rule 17a-11: Notification Provisions for Brokers and Dealers	Exchange Act Rule 18a-8
Exchange Act Rule 17a-13: Quarterly Security Counts to Be Made by Certain Exchange Members, Brokers and Dealers	Exchange Act Rule 18a-9

Appendix B

Note: This chart is taken from the chart that appears in the SEC's release except that we have added footnotes 1-17 to provide more detail as to the specific broker-dealer rule on which a newly proposed SBSD rule was based.

	Non-SBSD/ MSBSP broker-dealers	Non-model broker-dealer SBSDs	ANC broker- dealer SBSDs	Broker-dealer MSBSPs	Non-model stand-alone SBSDs	ANC stand- alone SBSDs	Bank SBSDs	Stand- alone MSBSPs
Trade blotters	17a-3(a)(1)*	17a-3(a)(1)*	17a-3(a)(1)*	17a-3(a)(1)*	18a-5(a)(1)	18a-5(a)(1)	18a-5(b)(1)	18a-5(a)(1)
General ledger					18a-5(a)(2)	18a-5(a)(2)		18a-5(a)(2)
Ledgers for customer and non-customer accounts	17a-3(a)(3)*	17a-3(a)(3)*	17a-3(a)(3)*	17a-3(a)(3)*	18a-5(a)(3)	18a-5(a)(3)	18a-5(b)(2)	18a-5(a)(3)
Stock record	17a-3(a)(5)*	17a-3(a)(5)*	17a-3(a)(5)*	17a-3(a)(5)*	18a-5(a)(4)	18a-5(a)(4)	18a-5(b)(3)	18a-5(a)(4)
Memoranda of brokerage orders	17a-3(a)(6)*	17a-3(a)(6)*	17a-3(a)(6)*	17a-3(a)(6)*			18a-5(b)(4)	
Memoranda of proprietary orders	17a-3(a)(7)*	17a-3(a)(7)*	17a-3(a)(7)*	17a-3(a)(7)*	18a-5(a)(5)	18a-5(a)(5)	18a-5(b)(5)	18a-5(a)(5)
Confirmations	17a-3(a)(8)*	17a-3(a)(8)*	17a-3(a)(8)*	17a-3(a)(8)*	18a-5(a)(6)	18a-5(a)(6)	18a-5(b)(6)	18a-5(a)(6)
Accountholder information	17a-3(a)(9)*	17a-3(a)(9)*	17a-3(a)(9)*	17a-3(a)(9)*	18a-5(a)(7)	18a-5(a)(7)	18a-5(b)(7)	18a-5(a)(7)
Options positions ¹⁴					18a-5(a)(8)	18a-5(a)(8)		18a-5(a)(8)
Trial balances and computation of net capital ¹⁵					18a-5(a)(9)	18a-5(a)(9)		18a-5(a)(9)
Associated person's employment application ¹⁶					18a-5(a)(10)	18a-5(a)(10)	18a-5(b)(8)	18a-5(a)(10)
Liquidity stress test			17a-3(a)(24)			18a-5(a)(11)		
Account equity and margin calculations under proposed Rule 18a-3		17a-3(a)(25)	17a-3(a)(25)	17a-3(a)(25)	18a-5(a)(12)	18a-5(a)(12)		18a-5(a)(12)
Possession or control requirements under proposed Rule 18a-4		17a-3(a)(26)	17a-3(a)(26)		18a-5(a)(13)	18a-5(a)(13)	18a-5(b)(9)	
Customer reserve requirements under proposed Rule 18a-4		17a-3(a)(27)	17a-3(a)(27)		18a-5(a)(14)	18a-5(a)(14)	18a-5(b)(10)	
Unverified transactions		17a-3(a)(28)	17a-3(a)(28)	17a-3(a)(28)	18a-5(a)(15)	18a-5(a)(15)	18a-5(b)(11)	18a-5(a)(15)
Political contributions		17a-3(a)(29)	17a-3(a)(29)		18a-5(a)(16)	18a-5(a)(16)	18a-5(b)(12)	
Compliance with external business conduct requirements		17a-3(a)(30)	17a-3(a)(30)	17a-3(a)(30)	18a-5(a)(17)	18a-5(a)(17)	18a-5(b)(13)	18a-5(a)(17)

¹⁴ New Exchange Act Rule 18a-5(a)(8) is based on existing Exchange Act Rule 17a-3(a)(5)

¹⁵ New Exchange Act Rule 18a-5(a)(9) is based on existing Exchange Act Rule 17a-3(a)(11)

¹⁶ New Exchange Act Rule 18a-5(a)(10) is based on existing Exchange Act Rule 17a-3(a)(12)(i)

	Non-SBSD/ MSBSP broker-dealers	Non-model broker-dealer SBSBs	ANC broker- dealer SBSBs	Broker-dealer MSBSPs	Non-model stand-alone SBSBs	ANC stand- alone SBSBs	Bank SBSBs	Stand- alone MSBSPs
Records to be preserved for a period of not less than 6 years								
Trade blotters ¹⁷					18a-6(a)(1) citing 18a-5(a)(1)	18a-6(a)(1) citing 18a-5(a)(1)	18a-6(a)(2) citing 18a-5(b)(1)	18a-6(a)(1) citing 18a-5(a)(1)
General ledger ¹⁸					18a-6(a)(1) citing 18a-5(a)(2)	18a-6(a)(1) citing 18a-5(a)(2)		18a-6(a)(1) citing 18a-5(a)(2)
Ledgers for customer and non-customer accounts ¹⁹					18a-6(a)(1) citing 18a-5(a)(3)	18a-6(a)(1) citing 18a-5(a)(3)	18a-6(a)(2) citing 18a-5(b)(2)	18a-6(a)(1) citing 18a-5(a)(3)
Stock record ²⁰					18a-6(a)(1) citing 18a-5(a)(4)	18a-6(a)(1) citing 18a-5(a)(4)	18a-6(a)(2) citing 18a-5(b)(3)	18a-6(a)(1) citing 18a-5(a)(4)
Records to be preserved for a period of not less than 3 years								
Memoranda of brokerage orders ²¹							18a-6 (b)(2)(i) citing 18a-6(b)(4)	
Memoranda of proprietary orders ²²					18a-6 (b)(1)(i) citing 18a-6(a)(5)	18a-6 (b)(1)(i) citing 18a-6(a)(5)	18a-6 (b)(2)(i) citing 18a-6(b)(5)	18a-6 (b)(1)(i) citing 18a-6(a)(5)
Confirmations ²³					18a-6 (b)(1)(i) citing 18a-6(a)(6)	18a-6 (b)(1)(i) citing 18a-6(a)(6)	18a-6 (b)(2)(i) citing 18a-6(b)(6)	18a-6 (b)(1)(i) citing 18a-6(a)(6)
Accountholder information					18a-6 (b)(1)(i) citing 18a-6(a)(7)	18a-6 (b)(1)(i) citing 18a-6(a)(7)	18a-6 (b)(2)(i) citing 18a-6(b)(7)	18a-6 (b)(1)(i) citing 18a-6(a)(7)
Options positions ²⁴					18a-6 (b)(1)(i) citing 18a-6(a)(8)	18a-6 (b)(1)(i) citing 18a-6(a)(8)		18a-6 (b)(1)(i) citing 18a-6(a)(8)

¹⁷ New Exchange Act Rules 18a-6(a)(1) and 18a-6(a)(2) are based on existing Exchange Act Rule 17a-4(a)

¹⁸ New Exchange Act Rule 18a-6(a)(1) is based on existing Exchange Act Rules 17a-4(a)

¹⁹ New Exchange Act Rule New Exchange Act Rules 18a-6(a)(1) and 18a-6(a)(2) are based on existing Exchange Act Rule 17a-4(a)

²⁰ New Exchange Act Rule New Exchange Act Rules 18a-6(a)(1) and 18a-6(a)(2) are based on existing Exchange Act Rule 17a-4(d)

²¹ New Exchange Act Rule New Exchange Act Rule 18a-6 (b)(2)(i) is based on existing Exchange Act Rules 17a-4(b)(7)

²² New Exchange Act Rule New Exchange Act Rule 18a-6 (b)(1)(i) is based on existing Exchange Act Rule 17a-4(b)(4)

²³ New Exchange Act Rule New Exchange Act Rules 18a-6 (b)(1)(i) and 18a-6 (b)(2)(i) are based on existing Exchange Act Rule 17a-4(b)(8)

²⁴ New Exchange Act Rule New Exchange Act Rule 18a-6 (b)(1)(i) is based on existing Exchange Act Rule 17a-4(b)(8)(ix)

	Non-SBSD/ MSBSP broker-dealers	Non-model broker-dealer SBSBs	ANC broker- dealer SBSBs	Broker-dealer MSBSPs	Non-model stand-alone SBSBs	ANC stand- alone SBSBs	Bank SBSBs	Stand- alone MSBSPs
Trial balances and computation of net capital	17a-4(b)(1) citing 17a-3(a)(11)	17a-4(b)(1) citing 17a-3(a)(11)	17a-4(b)(1) citing 17a-3(a)(11)	17a-4(b)(1) citing 17a-3(a)(11)	18a-6 (b)(1)(i) citing 18a-6(a)(9)	18a-6 (b)(1)(i) citing 18a-6(a)(9)		18a-6 (b)(1)(i) citing 18a-6(a)(9)
Liquidity stress test			17a-4(b)(1) citing 17a-3(a)(24)			18a-6 (b)(1)(i) citing 18a-6(a)(11)		
Account equity and margin calculations under proposed Rule 18a-3		17a-4(b)(1) citing 17a-3(a)(25)	17a-4(b)(1) citing 17a-3(a)(25)	17a-4(b)(1) citing 17a-3(a)(25)	18a-6 (b)(1)(i) citing 18a-6(a)(12)	18a-6 (b)(1)(i) citing 18a-6(a)(12)		18a-6 (b)(1)(i) citing 18a-6(a)(12)
Possession or control requirements under proposed Rule 18a-4		17a-4(b)(1) citing 17a-3(a)(26)	17a-4(b)(1) citing 17a-3(a)(26)		18a-6 (b)(1)(i) citing 18a-6(a)(13)	18a-6 (b)(1)(i) citing 18a-6(a)(13)	18a-6 (b)(2)(i) citing 18a-6(b)(9)	
Customer reserve requirements under proposed Rule 18a-4		17a-4(b)(1) citing 17a-3(a)(27)	17a-4(b)(1) citing 17a-3(a)(27)		18a-6 (b)(1)(i) citing 18a-6(a)(14)	18a-6 (b)(1)(i) citing 18a-6(a)(14)	18a-6 (b)(2)(i) citing 18a-6(b)(10)	
Unverified transactions		17a-4(b)(1) citing 17a-3(a)(28)	17a-4(b)(1) citing 17a-3(a)(28)	17a-4(b)(1) citing 17a-3(a)(28)	18a-6 (b)(1)(i) citing 18a-6(a)(15)	18a-6 (b)(1)(i) citing 18a-6(a)(15)	18a-6 (b)(2)(i) citing 18a-6(b)(11)	18a-6 (b)(1)(i) citing 18a-6(a)(15)
Political contributions		17a-4(b)(1) citing 17a-3(a)(29)	17a-4(b)(1) citing 17a-3(a)(29)		18a-6 (b)(1)(i) citing 18a-6(a)(16)	18a-6 (b)(1)(i) citing 18a-6(a)(16)	18a-6 (b)(2)(i) citing 18a-6(b)(12)	
Compliance with external business conduct requirements		17a-4(b)(1) citing 17a-3(a)(30)	17a-4(b)(1) citing 17a-3(a)(30)	17a-4(b)(1) citing 17a-3(a)(30)	18a-6 (b)(1)(i) citing 18a-6(a)(17)	18a-6 (b)(1)(i) citing 18a-6(a)(17)	18a-6 (b)(2)(i) citing 18a-6(b)(13)	18a-6 (b)(1)(i) citing 18a-6(a)(17)
Bank records ²⁵					18a-6 (b)(1)(ii)	18a-6 (b)(1)(ii)		18a-6 (b)(1)(ii)
Bills ²⁶					18a-6 (b)(1)(iii)	18a-6 (b)(1)(iii)		18a-6 (b)(1)(iii)
Communications	17a-4(b)(4)*	17a-4(b)(4)*	17a-4(b)(4)*	17a-4(b)(4)*	18a-6 (b)(1)(iv)	18a-6 (b)(1)(iv)	18a-6 (b)(2)(ii)	18a-6 (b)(1)(iv)
Trial balances ²⁷					18a-6 (b)(1)(v)	18a-6 (b)(1)(v)		18a-6 (b)(1)(v)
Account documents ²⁸					18a-6 (b)(1)(vi)	18a-6 (b)(1)(vi)	18a-6 (b)(2)(iii)	18a-6 (b)(1)(vi)
Written agreements	17a-4(b)(7)*	17a-4(b)(7)*	17a-4(b)(7)*	17a-4(b)(7)*	18a-6 (b)(1)(vii)	18a-6 (b)(1)(vii)	18a-6 (b)(2)(iv)	18a-6 (b)(1)(vii)
Information supporting financial reports	17a-4(b)(8)*	17a-4(b)(8)*	17a-4(b)(8)*	17a-4(b)(8)*	18a-6 (b)(1)(viii)	18a-6 (b)(1)(viii)	18a-6 (b)(2)(v)	18a-6 (b)(1)(viii)

²⁵ New Exchange Act Rule 18a-6 (b)(1)(ii) is based on existing Exchange Act Rule 17a-4(b)(2)

²⁶ New Exchange Act Rule 18a-6 (b)(1)(iii) is based on existing Exchange Act Rule 17a-4(b)(3)

²⁷ New Exchange Act Rule 18a-6 (b)(1)(v) is based on existing Exchange Act Rule 17a-4(b)(5)

²⁸ New Exchange Act Rule 18a-6 (b)(1)(vi) is based on existing Exchange Act Rule 17a-4(b)(6)

	Non-SBSD/ MSBSP broker-dealers	Non-model broker-dealer SBSBs	ANC broker- dealer SBSBs	Broker-dealer MSBSPs	Non-model stand-alone SBSBs	ANC stand- alone SBSBs	Bank SBSBs	Stand- alone MSBSPs
Rule 15c3-4 risk management records (OTC derivatives dealers only) ²⁹					18a-6 (b)(1)(ix)	18a-6 (b)(1)(ix)		18a-6 (b)(1)(ix)
Internal credit ratings						18a-6 (b)(1)(x)		
Regulation SBSR information	17a-4(b)(14)	17a-4(b)(14)	17a-4(b)(14)	17a-4(b)(14)	18a-6 (b)(1)(xi)	18a-6 (b)(1)(xi)	18a-6 (b)(2)(vi)	18a-6 (b)(1)(xi)
Records relating to business conduct standards		17a-4(b)(15)	17a-4(b)(15)	17a-4(b)(15)	18a-6 (b)(1)(xii)	18a-6 (b)(1)(xii)	18a-6 (b)(2)(vii)	18a-6 (b)(1)(xii)
Special entity documents		17a-4(b)(16)	17a-4(b)(16)	17a-4(b)(16)	18a-6 (b)(1)(xiii)	18a-6 (b)(1)(xiii)	18a-6 (b)(2)(viii)	18a-6 (b)(1)(xiii)
Associated person's employment application ³⁰					18a-6(d)(1)	18a-6(d)(1)	18a-6(d)(1)	18a-6(d)(1)
Regulatory authority reports ³¹					18a-6 (d)(2)(i)	18a-6 (d)(2)(i)	18a-6 (d)(2)(ii)	18a-6 (d)(2)(i)
Compliance, supervisory, and procedures manuals ³²					18a-6 (d)(3)(i)	18a-6 (d)(3)(i)	18a-6 (d)(3)(ii)	18a-6 (d)(3)(i)
Life of the enterprise and of any successor enterprise								
Corporate documents	17a-4(d)*	17a-4(d)*	17a-4(d)*	17a-4(d)*	18a-6(c)	18a-6(c)		18a-6(c)

* Broker-dealers are currently required to comply with these paragraphs of Rule 17a-4, but the Commission proposes to amend these paragraphs as required by the Dodd-Frank Act or to tailor to the types of records that should be preserved with respect to security-based swaps, and to make certain technical changes.

²⁹ New Exchange Act Rule 18a-6 (b)(1)(ix) is based on existing Exchange Act Rule 17a-4(e)(9)

³⁰ New Exchange Act Rule 18a-6(d)(1) is based on existing Exchange Act Rule 17a-4(e)(1)

³¹ New Exchange Act Rule 18a-6 (d)(2)(i) is based on existing Exchange Act Rule 17a-4(e)(6)

³² New Exchange Act Rule 18a-6 (d)(3)(i) is based on existing Exchange Act Rule 17a-4(e)(7)