

Final Rules: Regulatory Regime for Security-Based Swap Execution Facilities



The Securities and Exchange Commission adopted rules that:

- Create a regime for the registration and regulation of security-based swap execution facilities (SBSEFs);
- Address various issues relating to the “trade execution requirement” for security-based swaps (SBS), such as by setting out the cross-border application of that requirement;
- Address conflicts of interest at SBSEFs and national securities exchanges that trade SBS; and
- Promote consistency between the rules governing SBSEFs and existing rules under the Securities Exchange Act of 1934 (Exchange Act).

Why This Matters

To enhance transparency and oversight of the over-the-counter derivatives market, Title VII of the Dodd-Frank Act requires the Commission to implement a regulatory framework for SBS that requires the registration and regulation of SBSEFs and mitigates conflicts of interest on SBSEFs and SBS exchanges. The Commission adopted new Regulation SE to implement these statutory requirements, which is an important step in the SEC’s efforts to finalize its regulatory regime for the SBS market.

How the Rules Apply

Regulation SE creates a regime for the registration and regulation of SBSEFs. Key rules within Regulation SE establish a process for SBSEF registration; establish procedures for rule and product filings by SBSEFs; establish permissible execution methods for SBS that are subject to the Exchange Act’s trade execution requirement; set out a procedure for SBSEFs to make an SBS available to trade and establish certain exceptions from the trade execution requirement; implement the 14 Core Principles for SBSEFs set forth in section 3D(d) of the Exchange Act; address cross-border matters; and impose requirements addressing conflicts of interest involving SBSEFs and SBS exchanges.

The adopted rules and amendments also include provisions that:

- Deem a registered SBSEF (not otherwise engaging in other types of brokerage activity) to also be registered with the Commission as a broker, and exempt that SBSEF from certain broker requirements;

- Allow for Commission review of final actions taken by an SBSEF;
 - Exclude from the definition of “exchange” registered SBSEFs and registered SBS clearing agencies that perform certain matching and execution functions; and
 - Sunset certain existing temporary exemptions from registration as an SBSEF, national securities exchange, or clearing agency.
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What’s Required

For an entity meeting the definition of “security-based swap execution facility”:

- Register with the Commission as an SBSEF on Form SBSEF or register as a national securities exchange; and
- Foreign SBS trading venues may seek an exemption, pursuant to Rule 833(a), from the requirement to register.

A registered SBSEF must:

- Submit filings with the Commission for new rules, rule amendments, and products;
 - Establish and enforce compliance with its rules, which must include, among other things, rules regarding impartial access, trading and trade processing, the operation of the SBSEF, the financial integrity of SBS on its facility, the exercise of emergency authority, and conflicts of interest;
 - Monitor trading to prevent manipulation, price distortion, and delivery or settlement disruptions;
 - Make public timely information on price, trading volume, and other trading data on SBS transactions and publish on its website a Daily Market Data Report;
 - Maintain records of all activities of the facility, including a complete audit trail, in a form and manner acceptable to the Commission, for a period of five years;
 - Have adequate financial, operational, and managerial resources;
 - Establish and maintain a program of automated systems and risk analysis;
 - Establish and maintain emergency procedures, backup facilities, and a disaster recovery plan; and
 - Designate a chief compliance officer (CCO) and establish regulatory and reporting obligations for the CCO.
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What’s Next

The adopted rules will become effective 60 days following the date of publication in the Federal Register. Any entity that meets the definition of SBSEF may file an application to register with the Commission on Form SBSEF at any time after the effective date, and would need to do so within 180 days of the effective date and have its application on Form SBSEF be complete within 240 days of the effective date to continue to operate as an SBSEF while its application is pending.