

Client Update

SEC Final Rules on Registration of Security-Based Swap Entities and Proposed Rules on Statutorily Disqualified Associated Persons

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On August 5, 2015, the Securities and Exchange Commission (the “SEC”) issued final rules (the “Final Rules”)¹ establishing a process for security-based swap dealers (“SBSDs”) and major security-based swap participants (“MSBSPs” and together with SBSDs, “SBS Entities”) to register with the SEC, as required under Section 15F of the Securities Exchange Act of 1934 (the “Exchange Act”).

The Final Rules and the accompanying release (the “Adopting Release”) address, among other things, the content of the registration application and the appropriate form to be filed by various types of entities, the process for filing such an application and any amendment thereto, the certifications and due diligence required in connection with an application, the process for terminating an SBS Entity’s registration (including withdrawal from registration by the SBS Entity or revocation or cancellation of registration by the SEC), and certain additional requirements applicable to “nonresident” SBS Entities. The Final Rules also provide a limited exception to SBS Entities from the prohibition (the “Disqualified AP Prohibition”) against using a “statutorily disqualified” associated person (“AP”) in effecting the SBS Entity’s security-based swap transactions, which exception applies only to APs that are entities.

The Final Rules were published in the Federal Register on August 14, 2015, and will become effective on October 13, 2015. The compliance date and other

¹ The text of the Final Rules is available at <https://www.federalregister.gov/articles/2015/08/14/2015-19661/registration-process-for-security-based-swap-dealers-and-major-security-based-swap-participants>.

relevant dates with respect to the Final Rules are addressed in a separate section below.

In connection with the Final Rules, the SEC also issued proposed rules (the “Proposed AP Rules”)² on August 5, 2015, setting forth a process for SBS Entities to file an application with the SEC for permission to have statutorily disqualified APs effect or be involved in effecting security-based swaps on the SBS Entity’s behalf, despite the Disqualified AP Prohibition.

The Proposed AP Rules also provide temporary relief to SBS Entities from the Disqualified AP Prohibition with respect to a statutorily disqualified AP that is an entity, permitting an SBS Entity to continue using such a statutorily disqualified entity in effecting security-based swaps on its behalf for a limited period of time after the entity becomes so disqualified (or upon a statutorily disqualified entity becoming an AP of the SBS Entity) and during the pendency of the review of the SBS Entity’s application to continue using the AP in that manner.

Additionally, where the Commodity Futures Trading Commission (the “CFTC”), a self-regulatory organization (“SRO”) or a registered futures association (e.g., the National Futures Association (the “NFA”)) has granted a prior application or otherwise granted relief from a statutory disqualification with respect to the AP, the Proposed AP Rules provide a streamlined process for an SBS Entity to file a notice with the SEC in lieu of submitting an application to continue using the AP in effecting security-based swaps.

Comments on the Proposed AP Rules are due by October 26, 2015.

FINAL RULES ON REGISTRATION FOR SBS ENTITIES

Compliance Date and Counting Dates for Final Rules

To provide potential SBS Entities with the necessary time to review the rules the SEC adopts for SBS Entities before making decisions relating to business structure (such as whether they will continue to conduct a security-based swap business in the U.S.), and to determine which of their APs may be subject to the Disqualified AP Prohibition before they register, the SEC has adopted a compliance date for the Final Rules (the “Registration Compliance Date”) based

² The text of the Proposed AP Rules is available at: <https://www.sec.gov/rules/proposed/2015/34-75612.pdf>

on the date of publication or the compliance date of the other rules applicable to SBS Entities. Specifically, the Registration Compliance Date is the latest of:

- six months after the date of publication in the Federal Register of a final rule release adopting rules establishing capital, margin and margin segregation requirements for SBS Entities;
- the compliance date of final rules establishing recordkeeping and reporting requirements for SBS Entities;
- the compliance date of final rules establishing business conduct requirements under the Exchange Act for SBS Entities; or
- the compliance date for final rules establishing a process for a registered SBS Entity to make an application to the SEC to permit an associated person who is subject to a statutory disqualification to effect or be involved in effecting security-based swaps on its behalf.

For purposes of complying with the registration and other requirements applicable to SBS Entities, the Final Rules provide that persons are not required to begin determining whether their activities meet or exceed the applicable thresholds for SBS or MSBSP registration (under the joint final entity definition rules adopted by the SEC and the CFTC)³ until two months⁴ prior to the Registration Compliance Date (the “SBS Entity Counting Date”). Therefore, only security-based swap positions connected with the dealing activity in which the person (or any other entity controlling, controlled by or under common control with the person) engages on or after the SBS Entity Counting Date will count toward determining that person’s status as an SBS, and only positions held on or after the SBS Counting Date will count towards determining that person’s status as an MSBSP.

³ The rules applicable to SBS Entities are set forth in sections 3a71-2, 3a67-3 and 3a67-5 of the SEC rules. *See also* our client memorandum, “CFTC and SEC Release Joint Final Rule on Key Entity Definitions in Title VII of the Dodd-Frank Act,” dated June 8, 2012, available at http://www.debevoise.com/insights/publications/2012/06/cftc-and-sec-release-joint-final-rule-on-key-ent_].

⁴ As a general rule, if a person not registered as an SBS Entity can no longer rely on an exception from registration due to increased dealing activities or increased security-based swap positions (as applicable), such person will have two months following the end of the month in which it ceased to be able to rely on such exception to submit a completed registration application to the SEC.

Process for Registration as an SBS Entity

Forms of Application and Required Information

Under the Final Rules, an application for registration of an SBS Entity must be filed on one of the following forms, depending on the type of entity: Form SBSE-BD, Form SBSE-A, or Form SBSE.

- Form SBSE-BD: for an SBS Entity that has previously filed Form BD with the SEC to register as a broker-dealer.
- Form SBSE-A: for an SBS Entity that is filing or has previously filed Form 7-R with the CFTC (or its designee) to register as a swap dealer (“SD”) or major swap participant (“MSP”) and that is not also registered or registering with the SEC as a broker-dealer.
- Form SBSE: for all other SBS Entities.

Form SBSE

Form SBSE is generally based on Form BD (*i.e.*, the consolidated form used by broker-dealers to register with the SEC, states, and SROs) modified to account for differences between the broker-dealer and security-based swap businesses.

Form SBSE requires an applicant to provide general information about the applicant; a brief description of the applicant’s business; information regarding other regulators with which it may already be registered (including foreign regulators); information regarding the identity of persons who directly or indirectly control, are controlled by, or are under common control with the applicant and whether those persons are in the securities, investment advisory or banking businesses; and information regarding certain criminal, regulatory, civil judicial, and financial actions taken against the applicant and its control affiliates.

Form SBSE also includes certain schedules in which the applicant must provide, among other things, information on its direct and indirect owners; information regarding statutorily disqualified APs that are entities and that effect or are involved in effecting security-based swaps on the applicant’s behalf; and information on additional business locations of the applicant. In addition, nonresident applicants must complete Schedule F by providing information regarding the applicant’s U.S. agent for service of process and the foreign regulators with which the applicant may be registered, as well as a certification that the applicant can, as a matter of law, and will provide the SEC with prompt access to its books and records and submit to onsite examination by the SEC.

Form SBSE-A

Form SBSE-A is similar to, but shorter than, Form SBSE and is designed to facilitate the application process for dual SEC and CFTC registrants (*i.e.*, persons registered or applying for registration as both an SBS Entity and as an SD or MSP). Form SBSE-A provides the SEC with necessary data that is not included in the forms filed with the CFTC. An applicant that uses Form SBSE-A must also provide the SEC with a copy of the form it files with the CFTC to register as an SD or MSP.

Form SBSE-BD

Form SBSE-BD is designed to facilitate the application process for persons that are registered or applying for registration with the SEC as both an SBS Entity and as a broker or dealer. Form SBSE-BD is significantly shorter than both Form SBSE and Form SBSE-A, and is intended to provide the SEC with data not included on the Form BD.

Senior Officer and CCO Certifications on Form SBSE-C

In addition to the application filed on Form SBSE, SBSE-A or SBSE-BD, the Final Rules require that all applicants for registration as an SBS Entity must file a Form SBSE-C consisting of two separate certifications described below.

Senior Officer Certification

All applicants for registration as an SBS Entity must include in their Form SBSE-C a certification by a “senior officer” of the applicant (with legal authority to bind the applicant) that: (1) after due inquiry, he or she has reasonably determined that the applicant has developed and implemented written policies and procedures reasonably designed to prevent violation of federal securities laws and the rules thereunder, and (2) he or she has documented the process by which he or she reached such determination.

In the Adopting Release, the SEC clarifies that “senior officer” for these purposes is meant to cover only “the most senior executives in the organization,” such as the SBS Entity’s chief executive officer, chief financial officer, chief legal officer, chief compliance officer, president, or other person at a similar level who has the authority to bind such SBS Entity.

The SEC clarifies in the Adopting Release that the requirement to conduct “due inquiry” means that the senior officer who makes the certification on Form SBSE-C should conduct diligence regarding the content of what the senior officer is required to certify. However, the SEC notes that SBS Entities should

have flexibility in determining the steps that the senior officer should take to conduct such diligence (including reviewing the SBS Entity's written policies and procedures and/or speaking with the SBS Entity's legal and compliance personnel regarding such policies and procedures and their implementation).

Further, the SEC states that this senior officer certification requirement differs from the CFTC's rules for registration of SDs and MSPs because all CFTC swap registrants are required to be members of the NFA and so are subject to the additional registration review process and oversight of an SRO, while SBS Entities are currently not required to become members of any SRO and so will not be subject to similar oversight.

Certification Regarding Associated Persons

The Final Rules also require applicants for registration as an SBS Entity to include in their SBSE-C, a certification (the "AP Certification") that the SBS Entity neither knows, nor in the exercise of reasonable care should have known, that any person associated with the SBS Entity who effects or is involved in effecting security-based swaps on behalf of the SBS Entity is subject to "statutory disqualification," unless otherwise specifically provided by rule, regulation or order of the SEC.

We discuss in a separate section below this certification requirement and related due diligence requirements, as well as the meaning of the term "statutory disqualification," the Disqualified AP Prohibition and a limited exception to this prohibition.

Conditional Registration

An applicant for registration will be automatically considered to be conditionally registered as an SBS Entity upon filing a complete application with the SEC (consisting of a Form SBSE, SBSE-A, or SBSE-BD, as well as a Form SBSE-C) within the prescribed time period for SBS or MSBSP registration (as applicable), and will continue to be conditionally registered until the SEC grants or denies the entity's ongoing registration (or the SBS Entity withdraws its registration).

Standards for Granting or Denying Ongoing Registration as an SBS Entity

The Final Rules provide that the SEC may grant or deny ongoing registration to an applicant based on the SBS Entity's application.⁵ The SEC will grant ongoing

⁵ The SEC notes in the Adopting Release that it intends to notify entities electronically through the EDGAR system when registration is granted, and will make information regarding registration status publicly available on EDGAR.

registration to an SBS Entity if it finds that the SBS Entity has satisfied the requirements of Section 15F(b) of the Exchange Act, which is the statutory provision requiring applicants to file a registration application with the SEC containing such information as the SEC considers necessary concerning the business in which the applicant is or will be engaged.

The Final Rules further provide that the SEC may institute proceedings to determine whether ongoing registration should be denied if:

- the SEC does not or cannot make a finding that the requirements of Section 15F(b) are satisfied;
- the applicant is subject to a statutory disqualification (as described in Sections 3(a)(39)(A) through (F) of the Exchange Act and discussed below); or
- the SEC is aware of inaccurate statements in the application.

Such proceedings will include notice of the grounds for denial under consideration and opportunity for hearing. The applicant will have the chance (once proceedings are commenced) to provide information as to why the SEC should grant ongoing registration. At the conclusion of the proceedings, the SEC will grant or deny ongoing registration.

Amendments to Application Forms

Under the Final Rules, if an SBS Entity finds that the information contained in its Form SBSE, Form SBSE-A, or Form SBSE-BD, or in any amendment thereto, is or has become inaccurate for any reason, the SBS Entity must promptly file an amendment to the appropriate Form (through the SEC's EDGAR system) to correct such information. The SEC indicates in the Adopting Release that it believes that it would be appropriate to interpret "promptly" to mean within 30 days. The SEC also clarifies in the Adopting Release that the certifications on Form SBSE-C are one-time certifications, and that a Form SBSE-C therefore need not be amended.

Termination of Registration

An SBS Entity that is registered with the SEC will continue to be registered until such registration is withdrawn, revoked, or canceled.

Withdrawal

The Final Rules provide that to withdraw from registration, a registered SBS Entity must file a notice of withdrawal on Form SBSE-W electronically through the EDGAR system. In addition, prior to filing its notice of withdrawal on Form SBSE-W, the SBS Entity must amend its Form SBSE, Form SBSE-A, or Form SBSE-BD, as appropriate, to update any inaccurate information.

Among other general information, Form SBSE-W requires a registered SBS Entity to provide the date the SBS Entity ceased doing security-based swap business; the reason the SBS Entity is seeking to withdraw from SEC registration; whether the SBS Entity holds any segregated counterparty collateral; if the SBS Entity is the subject of, or named in, any investment-related investigations, customer-initiated complaints, or private civil litigations; and the location where the SBS Entity's books and records will be located, and who will have custody of those records.

Under the Final Rules, a notice of withdrawal from registration generally becomes effective on the 60th day after the SBS Entity files a Form SBSE-W. However, the SEC may extend the effective date of withdrawal to such later date as to which the SBS Entity consents or which the SEC by order may determine as necessary or appropriate in the public interest or for the protection of investors.

In addition, if either before the filing of a notice of withdrawal or prior to the effective date of such a withdrawal, the SEC institutes a proceeding to censure, place limitations on the activities, functions, or operations of, or suspend or revoke the registration of the SBS Entity, or to impose terms or conditions upon the SBS Entity's withdrawal, the notice of withdrawal will not become effective except at such time and upon such terms and conditions as the SEC deems necessary or appropriate in the public interest or for the protection of investors.

Cancellation and Revocation

The Final Rules provide that the SEC will, by order, cancel the registration of an SBS Entity if the SEC finds that such entity is no longer in existence or has ceased to do business as an SBS Entity.

In addition, the Final Rules provide that the SEC, by order, will censure, place limitations on the activities, functions, or operations of, or revoke the registration of any SBS Entity that has registered with the SEC if it makes a finding as specified in Section 15F(1)(2) of the Exchange Act. Specifically, the SEC will take such actions if it makes a definitive finding that:

- such censure, placing of limitations or revocation is in the public interest; and
- such SBS Entity or any AP of the SBS Entity effecting or involved in effecting security-based swap transactions on behalf of such SBS Entity (whether prior or subsequent to becoming an AP of the SBS Entity) (1) has committed or omitted, or is subject to orders or findings pertaining to, certain enumerated acts (including willfully making false or misleading statements in its registration application or in any report required to be filed with the SEC, omitting any material fact or willfully violating or aiding and abetting in the violation of certain federal securities or commodities laws and regulations), (2) has been convicted within 10 years of the commencement of the proceedings of certain enumerated felonies, misdemeanors or equivalent crimes (*i.e.*, crimes involving dishonesty or arising out of the conduct of the business of a broker, dealer, investment adviser, bank, insurance company, or certain other types of entities), (3) is subject to a permanent or temporary injunction against acting as a broker, dealer, investment adviser, or SBS Entity or in certain other securities-related capacities, (4) is subject to certain specified orders barring it from acting as a broker, dealer, or SBS Entity or in certain other securities-related capacities or (5) has been found by a foreign financial regulatory authority to have made false or misleading statements in any application for registration or report required to be filed with such regulator, or to have violated certain securities or commodities-related foreign statutes or regulations.

Associated Persons

Disqualified AP Prohibition

Section 15F(b)(6) of the Exchange Act prohibits an SBS Entity from permitting any person associated with the SBS Entity (*i.e.*, an AP) that is subject to a “statutory disqualification” to effect or be involved in effecting security-based swaps on behalf of the SBS Entity, if the SBS Entity knew, or in the exercise of reasonable care should have known, of the AP’s statutory disqualification (the “Disqualified AP Prohibition”).⁶

⁶ In 2011, the SEC issued an Order that, among other things, granted temporary relief from compliance with Section 15F(b)(6) of the Exchange Act, as well as Section 29(b) of the Exchange Act, concerning enforceability of contracts that would violate, among other provisions, Section 15F(b)(6). See Exchange Act Release No. 64678 (Jun. 15, 2011), 76 FR 36287, 36299-300 (Jun. 22, 2011). That Order expires on the effective date of the Final Rules. The SEC states in the Adopting Release that it will consider separately extending the expiration date of the temporary relief.

The term “statutory disqualification” is not specifically defined for the purposes of Section 15F(b)(6), but the SEC notes in the Adopting Release that the term has an established meaning under Section 3(a)(39) of the Exchange Act, which defines statutory disqualification with respect to membership or participation in an SRO; accordingly, the SEC clarifies that a person would be subject to a “statutory disqualification” under Section 15F(b)(6) if such person would be subject to “statutory disqualification” from association with a member of an SRO under Section 3(a)(39).⁷

The Exchange Act defines “persons associated with” an SBS Entity to include (1) any partner, officer, director, or branch manager of an SBS Entity (or any person occupying a similar status or performing similar functions); (2) any person directly or indirectly controlling, controlled by, or under common control with an SBS Entity; or (3) any employee of an SBS Entity. Since the term “person” is defined to include both entities and natural persons, the Disqualified AP Prohibition in the Exchange Act applies with respect to any statutorily disqualified AP, whether an entity or a natural person.

Limited Exception for Associated Persons That Are Entities

The Final Rules provide a limited exception from the Disqualified AP Prohibition for newly registered SBS Entities, which exception applies only with respect to APs that are entities. Specifically, under the Final Rules, unless otherwise ordered by the SEC, when filing a registration application, an SBS Entity may permit a person associated with the SBS Entity who is subject to a statutory disqualification to effect or be involved in effecting security-based swaps on behalf of the SBS Entity if:

1. The AP is not a natural person;
2. The statutory disqualification occurred prior to the compliance date of the Final Rules; and

⁷ “Statutory disqualification” for these purposes may be triggered by, among other things, certain convictions or adverse court findings; certain specified injunctions; expulsion or suspension from membership (or from being an AP of a member) of an SRO, securities or futures exchange or other trading platform; certain orders of the SEC, the CFTC or another regulatory agency denying, suspending or revoking registration as (or barring or suspending a person from being an AP of) a broker, dealer, SBS Entity, SD or MSP or certain other types of registered entity categories; or willfully making a false or misleading statement in any application for membership in an SRO or in any report filed with an SRO.

3. The SBS Entity identifies each such AP on Schedule C of its Form SBSE, Form SBSE-A, or Form SBSE-BD, as appropriate.

In the Adopting Release, the SEC notes that the Disqualified AP Prohibition and this exception apply not only to persons “effecting” security-based swap transactions (which includes persons engaging in a range of activities, including identification of potential purchasers, transmission or execution of orders, and clearance, settlement or confirmation of transactions), but also to persons “involved in effecting” such transactions. The SEC interprets the phrase “involved in effecting” to cover functions necessary to facilitate the SBS Entity’s security-based swap business (*i.e.*, activities directly related to key aspects of the overall process for effecting security-based swaps), including but not limited to (1) drafting and negotiating master agreements and confirmations; (2) recommending security-based swap transactions to counterparties; (3) being involved in executing security-based swap transactions on a trading desk;⁸ (4) pricing security-based swap positions; (5) managing collateral for the SBS Entity; and (6) directly supervising persons engaged in the foregoing activities.

In the Adopting Release, the SEC explains that this exception is designed to provide transitional relief for SBS entities, ensuring a smooth registration process and minimizing the potential for market disruptions. The Adopting Release states that the exception does not extend to natural persons because replacing a natural person responsible for negotiating or executing security-based swaps does not create the same practical issues as moving the services provided by an AP that is an entity to another entity.

In addition, the Proposed AP Rules, if adopted, would provide a mechanism for statutorily disqualified APs (whether entities or natural persons) to apply to the SEC to permit the AP to effect or be involved in effecting security-based swaps on the SBS Entity’s behalf, as well as a set of temporary exclusions from the Disqualified AP Prohibition for statutorily disqualified APs that are entities.

AP Certification Requirement

As noted above, the Final Rules require applicants for registration as an SBS Entity to include in their SBSE-C a certification that the SBS Entity neither knows, nor in the exercise of reasonable care should have known, that any person associated with the SBS Entity who effects or is involved in effecting

⁸ The SEC clarifies in the Adopting Release that there is no minimum amount of trading a person working on a trading desk must be involved with to be considered “involved in effecting” security-based swaps, and that the SEC’s focus is generally on the type of activity, not the amount of activity.

security-based swaps on behalf of the SBS Entity is subject to “statutory disqualification,” unless otherwise specifically provided by rule, regulation or order of the SEC.

The Final Rules further require that, to support the AP Certification, the SBS Entity’s Chief Compliance Officer (“CCO”), or his or her designee, must review and sign the questionnaire or application for employment (which the SBS Entity is required to obtain pursuant to the relevant recordkeeping rule applicable to such SBS Entity), executed by each AP who is a natural person⁹ and who effects or is involved in effecting security-based swaps on the SBS Entity’s behalf.

The SEC notes that the required employment questionnaire or application for natural persons includes a significant amount of information that may be helpful to determine whether an AP is subject to statutory disqualification, and that in some cases, calling past employers and checking references may be sufficient, while in other circumstances, a firm may decide to take additional steps. In addition, the SEC notes that for an SBS Entity whose associated persons are also associated with an affiliated broker-dealer, CFTC-registered entity, or bank, there may be circumstances where the SBS Entity and its CCO may rely on current background checks of dual employees performed by an affiliated, regulated entity as long as the other entity’s background check is sufficient for the SBS Entity to make the AP Certification.

Special Requirements for Nonresident SBS Entities

The Final Rules impose certain additional requirements on “nonresident” SBS Entities, including a requirement to obtain a U.S. agent for service of process and a requirement to provide a written certification and an opinion of counsel regarding the SEC’s access to the SBS Entity’s books and records and onsite examination of the SBS Entity by the SEC.

Definition of “Nonresident”

An SBS Entity is a “nonresident” under the Final Rules if:

- in the case of an individual, he or she resides, or has his or her principal place of business, in any place not in the United States;

⁹ Only natural persons would fill out such a questionnaire or application, so the CCO (or his or her designee) only must review and sign questionnaires or applications for associated persons that are natural persons.

- in the case of a corporation, it is incorporated in or has its principal place of business in any place not in the United States; or
- in the case of a partnership or other unincorporated organization or association, it has its principal place of business in any place not in the United States.

U.S. Agent for Service of Process

Under the Final Rules, a nonresident SBS Entity registered or applying for registration with the SEC must obtain a written irrevocable consent and power of attorney appointing an agent in the United States for service of process, pleadings or other papers in any action brought against the nonresident SBS Entity to enforce the Exchange Act. This consent and power of attorney must be signed by the agent and the nonresident SBS entity and maintained by the SBS Entity as part of its books and records for at least three years after the agreement is terminated. In addition, as part of its registration application, a nonresident SBS Entity must also provide the SEC with the name and address of the agent on Schedule F to its Form SBSE, Form SBSE-A, or Form SBSE-BD, as applicable.

In addition, the Final Rules require that any change with respect to a nonresident SBS Entity's US agent for service of process must be promptly communicated to the SEC.

Access to Books and Records and Onsite Examination of Nonresident SBS Entities

Under the Final Rules, a nonresident SBS Entity must also certify on Schedule F to Form SBSE, Form SBSE-A, or Form SBSE-BD (as applicable) that it can, as a matter of law, and will (1) provide the SEC with prompt access to the SBS Entity's books and records and (2) submit to onsite inspection and examination by the SEC. In addition, to support such certification, a nonresident SBS Entity must obtain an opinion of counsel that the SBS Entity can, as a matter of law, provide such prompt access to its books and records and submit to such examination.

If there is any change in the legal or regulatory framework that would impact the nonresident SBS Entity's ability to provide, or the manner in which it provides the SEC with prompt access to its books and records, or would impact the SEC's ability to inspect and examine the entity, such SBS Entity must, within 90 days of such change, re-certify the foregoing on Schedule F (to the appropriate application form) and provide a revised opinion of counsel describing how, as a matter of law, the nonresident SBS Entity will continue to

meet its obligations to provide the SEC with access to its books and records and to be subject to the SEC's inspection and examination under the new regulatory regime.

Special Situations

Succession

The Final Rules provide a process by which an SBS Entity may succeed to the business of another SBS Entity in a manner that ensures the registration requirements are satisfied during the transition. Specifically, if an SBS Entity succeeds to and continues the business of another SBS Entity, the registration of the predecessor SBS Entity would remain effective as the registration of the successor if the successor files an application for registration within 30 days after such succession, and the predecessor files a notice of withdrawal from registration on Form SBSE-W.

For a successor SBS Entity that succeeds to the business of another SBS Entity, where the ownership or control of the SBS Entity does not change (*i.e.*, the succession is based solely on a change in the predecessor's date or state of incorporation, form of organization, or composition of a partnership), the successor need not file a separate registration application and may instead amend the registration of the predecessor on Form SBSE, Form SBSE-A, or Form SBSE-BD (as appropriate) within 30 days after the succession.

Insolvency

The Final Rules provide a process by which an executor, administrator, receiver, bankruptcy trustee or other similar fiduciary of an insolvent SBS Entity (appointed or qualified by order, judgment or decree of a court of competent jurisdiction to continue the business of such SBS Entity) may continue the business of an SBS Entity for the period of time needed to close out positions or wind down the SBS Entity's business, if such fiduciary files with the SEC, within 30 days after entering upon the performance of his or her duties, an amended Form SBSE, Form SBSE-A, or Form SBSE-BD (as appropriate) indicating the fiduciary's position with respect to management of the SBS Entity, along with a copy of the order, judgment, decree, or other document appointing the fiduciary.

No Substituted Compliance

The SEC confirms in the Adopting Release that substituted compliance will not be available with respect to registration requirements for SBS Entities. Therefore, foreign registered SBS Entities will not be permitted to satisfy the SEC's

registration requirements by complying with the relevant registration requirements of their home jurisdiction (in lieu of complying with the SEC's registration requirements). However, the SEC notes that it intends to consider the potential availability of substituted compliance in connection with other requirements applicable to SBS Entities when it considers final rules to implement those requirements.

PROPOSED RULES ON APPLICATIONS BY SBS ENTITIES FOR STATUTORILY DISQUALIFIED ASSOCIATED PERSONS

To provide a procedure for parties to seek relief from the Disqualified AP Prohibition in the Final Rules, the SEC has concurrently issued Proposed AP Rules setting forth a process for SBS Entities to file an application (a "Disqualified AP Application") with the SEC for permission to have statutorily disqualified APs (both entities and natural persons) effect or be involved in effecting security-based swaps on the SBS Entity's behalf.

The Proposed AP Rules provide temporary relief to SBS Entities from the Disqualified AP Prohibition with respect to a statutorily disqualified AP that is not a natural person,¹⁰ permitting an SBS Entity to continue using such a statutorily disqualified AP in effecting security-based swaps on its behalf:

- for 30 days following the AP becoming subject to a statutory disqualification or for 30 days following a person that is subject to a statutory disqualification becoming an AP of an SBS Entity; and
- for 180 days following the filing a Disqualified AP Application if the application and certain required notices are filed within the 30-day period; or
- for 180 days following the filing of a complete application with, or initiation of a process by, the CFTC, an SRO or a registered futures association with respect to the AP for membership, association, registration or listing as a principal (pending a final decision with respect to any application or process) where the application has been filed, or the process started, prior to or within the same 30-day period, and a notice to the SEC has been filed within the same 30-day period.

¹⁰ The temporary relief does not apply with respect to APs that are natural persons, and is not available where the SEC, the CFTC, a registered futures association (such as the NFA) or an SRO has previously (1) issued an order contrary to such an exclusion (e.g., where the SEC, by order, has censured, placed limitations on the activities or functions of the AP or suspended or barred the person from being associated with an SBS Entity) or (2) denied membership, association, registration or listing as a principal with respect to the AP.

- The Proposed AP Rules further provide that if the SEC does not render a decision within either of the 180-day periods described above, the SBS Entity will have an additional 60 days to comply with the Disqualified AP Prohibition (*i.e.*, to make the changes necessary to ensure that the disqualified AP is not involved in effecting security-based swaps on behalf of the SBS Entity), unless the SEC extends the relief by order.

Finally, the Proposed AP Rules provide a streamlined process for an SBS Entity to continue using a statutorily disqualified AP in effecting security-based swaps by filing a notice with the SEC in lieu of submitting a Disqualified AP Application, where the SEC, the CFTC, an SRO (such as FINRA or a national securities exchange) or a registered futures association (such as the NFA) has granted a prior application or otherwise granted relief from a statutory disqualification with respect to the AP.

Application Process for Associated Persons Subject to Statutory Disqualification

The SEC sets forth in the Proposed AP Rules and accompanying release (the “Proposing AP Release”) the process for an SBS Entity to file a Disqualified AP Application for an SEC order (an “SEC Order”) under proposed Rule of Practice 194, permitting the SBS Entity to have a statutorily disqualified AP effect or be involved in effecting security-based swaps on behalf of the SBS Entity.

Required Showing

Under the Proposed AP Rules, the SBS Entity must show that it would be consistent with the public interest to permit the statutorily disqualified AP to effect or be involved in effecting security-based swaps on its behalf. To meet this burden, the SBS Entity’s Disqualified AP Application and supporting documentation must demonstrate that the terms or conditions of association, procedures, or proposed supervision (if the AP is a natural person) with respect to the AP are reasonably designed to ensure that the statutory disqualification does not negatively impact the ability of the AP to effect or be involved in effecting security-based swaps on behalf of the SBS Entity in compliance with applicable statutory and regulatory framework.

Form of Application

The Proposed AP Rules require that an SBS Entity’s Disqualified AP Application include certain exhibits, which differ depending on whether the application is filed with respect to an AP that is a natural person or an entity.

All Disqualified AP Applications with respect to any statutorily disqualified AP (whether a natural person or an entity) must include the following exhibits:

1. A copy of the order or other applicable document that resulted in the AP being subject to a statutory disqualification;
2. An undertaking by the SBS Entity to notify the SEC promptly in writing if any information submitted in support of the application becomes materially false or misleading while the application is pending; and
3. If the AP has been the subject of any proceeding resulting in the imposition of disciplinary sanctions during the five years preceding the filing of the application or is the subject of a pending proceeding by the SEC, the CFTC, any federal or state regulatory or law enforcement agency, registered futures association, foreign financial regulatory authority, registered national securities association or any other SRO, or commodities exchange, or any court, a copy of any order, decision, or document issued by the court, agency, SRO or other relevant authority involved.¹¹

In addition to exhibits 1-3 above, the Proposed AP Rules require that a Disqualified AP Application with respect to an AP that is a natural person must include the questionnaire or application for employment with respect to the AP (containing the AP's background information and disciplinary history).

In addition to exhibits 1-3 above, the application with respect to an AP that is an entity must include the following exhibits:

- Organizational charts of the AP, if available;
- Policies and procedures relating to the conduct resulting in the statutory disqualification that the AP has in place to ensure compliance with the federal or state securities laws, the Commodity Exchange Act, the CFTC rules thereunder, or the rules of the Municipal Securities Rulemaking Board, any SRO, or any foreign regulatory authority, as applicable ("AP Policies and Procedures"); and
- The names of any natural persons employed by the AP that are subject to a statutory disqualification and that would effect or be involved in effecting

¹¹ The SEC notes in the Proposing AP Release that where an AP has a history of misconduct, in addition to the conduct that triggered the statutory disqualification, the SEC generally would be less likely to grant an SEC Order with respect to such AP.

security-based swaps on behalf of the SBS Entity, as well as an indication of whether each such individual is an officer, partner, direct or indirect owner of the AP.

Written Statement

The Proposed AP Rules require that an SBS Entity's Disqualified AP Application must be supported by a written statement, signed by a knowledgeable person authorized by the SBS Entity, addressing certain items which differ depending on whether the application is filed with respect to an AP that is a natural person or an entity.

The written statement with respect to any statutorily disqualified AP (whether a natural person or an entity) must address each of the following:

1. The AP's compliance with any order resulting in statutory disqualification, including whether the AP has paid fines or penalties, disgorged monies, made restitution or paid any other monetary compensation required by any such order;
2. The capacity or position in which the AP proposes to be associated with the SBS Entity, including a description of the proposed duties of the AP;
3. The SBS Entity's compliance and disciplinary history during the five years preceding the filing of the Disqualified AP Application;
4. A detailed statement of why the AP should be permitted to effect or be involved in effecting security-based swaps on behalf of the SBS Entity, including what steps the AP or the SBS Entity has taken, or will take, to ensure that the statutory disqualification does not negatively impact upon the ability of the AP to effect or be involved in effecting security-based swaps on behalf of the SBS Entity in compliance with the applicable statutory and regulatory framework;
5. Whether the AP has been involved in any litigation during the five years preceding the filing of the Disqualified AP Application, or whether there are any unsatisfied judgments outstanding against the AP, in each case concerning investment or investment-related activities, and if so, details regarding such litigation or unsatisfied judgments; and
6. Any other information that the SBS Entity believes to be material to the application.

In addition to items 1-6 above, the written statement with respect to an AP that is a natural person must include the following:

- The AP's employment during the period subsequent to the issuance of the statutory disqualification;
- The terms and conditions of employment and supervision to be exercised over such AP and, where applicable, by such AP;
- The qualifications, experience, and disciplinary history of the proposed supervisor(s) of the AP;
- The names of any other APs of the SBS Entity who have previously been subject to a statutory disqualification and whether they are to be supervised by the AP; and
- Any relevant courses, seminars, examinations or other actions completed by the AP subsequent to becoming subject to a statutory disqualification to prepare for participation in the security-based swap business.

In addition to items 1-6 above, the written statement with respect to an AP that is an entity must include the following:

- General background information about the AP, including number of employees, number and location of offices, the types of businesses in which the AP is engaged, and any SRO memberships of the AP and the effective dates of membership; and
- A description of whether, with respect to the statutory disqualification and the sanctions imposed, the AP was ordered to undertake any changes to its organizational structure or AP Policies and Procedures, and if so, a description of what changes were mandated and whether the AP has implemented them.

Prior Applications or Processes

In addition to the exhibits and the appropriate written statement specified above, the Proposed AP Rules require that any SBS Entity filing a Disqualified AP Application must also provide the SEC with any order, notice or other applicable document reflecting the grant, denial, or other disposition (including dispositions on appeal) of any prior application or process concerning the AP by the SEC (pursuant to the Proposed AP Rules or similar rules providing a process to apply for relief from restrictions on acting in certain capacities or from

membership or association with certain persons),¹² by an SRO (following a proceeding for a person to become or remain a member, or an AP of a member, notwithstanding the existence of a statutory disqualification), or by the CFTC or a registered futures association (such as the NFA), where the prior application was for registration, including as an AP, or listing as a principal, notwithstanding the AP's statutory disqualification.¹³

Notice of Adverse Recommendation to the SBS Entity

Under the Proposed AP Rules, if SEC staff makes an adverse recommendation with respect to an SBS Entity's Disqualified AP Application, the SEC will notify the SBS Entity of such recommendation and provide a written statement of the reasons therefor. The SBS Entity will have 30 days to submit a written statement in response.

Notice in Lieu of an Application

In recognition of the regulatory efforts of the CFTC, NFA, and SROs with respect to APs within their jurisdiction, the Proposed AP Rules provide a process for SBS Entities to obtain relief from the Disqualified AP Prohibition by filing a notice with the SEC in lieu of a Disqualified AP Application, where the SEC, CFTC, NFA, or an SRO has granted a prior application or otherwise granted relief from a statutory disqualification with respect to the AP. Specifically, the Proposed AP Rules provide that an SBS Entity may permit a statutorily disqualified AP to effect or be involved in effecting security-based swaps on its behalf, without filing a Disqualified AP Application, if the SBS Entity has filed an AP Notice (as defined below) with the SEC and the following conditions are satisfied:

¹² The Proposed AP Rules provide that this includes grants, denials or other dispositions by the SEC of applications under Rule of Practice 193, section 9(c) of the Investment Company Act, section 19(d) of the Exchange Act and section 19h-1 of the SEC rules, each of which sets forth certain processes to apply to the SEC for relief from certain restrictions or disqualifications from acting or registering in certain capacities (e.g., broker, dealer, municipal securities dealers), from membership or participation in an SRO or from association with certain registered entities (e.g., brokers, dealers, investment companies, investment advisers) or SRO members.

¹³ The Proposed AP Rules provide that such CFTC dispositions include (1) any order or other document providing that the AP may be listed as a principal or registered as an AP of a CFTC registrant notwithstanding that the person is subject to a statutory disqualification from registration under sections 8a(2) and 8a(3) of the Commodity Exchange Act and (2) any determination by the NFA that had the AP applied for registration as an AP of an SD or MSP notwithstanding statutory disqualification, the application would have been granted or denied.

- The SEC, CFTC, NFA, or an SRO has specifically reviewed the underlying basis for the statutory disqualification (*i.e.*, all matters giving rise to the disqualification) and has made an affirmative determination concerning the AP to grant or otherwise approve membership, association, registration, or listing as a principal, notwithstanding the statutory disqualification;
- The terms and conditions of the association with the SBS Entity (*e.g.*, supervisory requirements) are the same in all material respects as those approved by the SEC, CFTC, NFA, or SRO in connection with the previous order, notice or other document granting membership, association, registration or listing as a principal;
- One of the following applies:
 - The AP has been admitted to or continued in membership, or participation or association with a member, of an SRO, notwithstanding that such person is subject to a statutory disqualification under 3a(39)(A) through (F) of the Exchange Act;
 - The AP is a natural person that has been granted consent by the SEC under Rule of Practice 193 to associate with a broker, dealer, investment adviser, investment company or other SEC registrant despite being barred by SEC order from such association;
 - The AP has been permitted to effect or be involved in effecting security-based swaps on behalf of an SBS Entity under the Proposed AP Rules (*e.g.*, where an SEC Order has been granted with respect to the AP, and the same AP becomes an AP of a different SBS Entity); or
 - The AP has been registered as, registered as an AP of or listed as a principal of, a CFTC registrant¹⁴ notwithstanding that the person is subject to statutory disqualification under sections 8a(2) and 8a(3) of the Commodity Exchange Act, provided that the AP is not subject to an SEC bar or suspension pursuant to sections 15(b), 15B, 15E, 15F or 17A of the Exchange Act, section 9(b) of the Investment Company Act of 1940 or section 203(f) of the Investment Advisers Act of 1940; and

The notice to the SEC (the “AP Notice”) must include the name of the SBS Entity and the name of the statutorily disqualified AP, and must identify the agency, SRO or registered futures association that has indicated its agreement

¹⁴ This includes persons registered as, registered as an AP of, or listed as a principal of, a futures commission merchant, retail forex dealer, introducing broker, commodity pool operator, commodity trading advisor or leverage transaction merchant, as well as persons registered as a floor broker or floor trader.

with the terms and conditions of the proposed association, registration or listing as a principal.

Where the disqualified AP is a natural person, the AP Notice must also include the name of the AP's prospective supervisor at the SBS Entity and the AP's place of employment.

Proposed Note

In a note attached as an appendix to the Proposed AP Rules (the "Proposed Note"), the SEC provides guidance to future SBS Entities regarding the importance of having adequate supervision in place to minimize the risk of future misconduct. The SEC stresses in the Proposed Note that the nature of the supervision that an AP will receive or exercise (as an AP of the SBS Entity) is an "important matter bearing upon the public interest," and that the SEC would therefore be less likely to issue an SEC Order where the AP is not subject to adequate supervision (particularly if the AP is supervised by another statutorily disqualified person) and where the AP supervises other persons (particularly if those persons are also subject to statutory disqualification).

The Proposed Note further provides that the SEC is unlikely to grant an SEC Order with respect to a statutorily disqualified AP seeking to become the sole proprietor of a registered SBS Entity due to the absence of supervision for such AP.

In addition, the Proposed Note provides that the SEC may decide to impose limitations on an SEC Order, such that an AP may be limited to association in a specified capacity with a particular registered SBS Entity and may also be subject to specific terms and conditions on such association (such as heightened supervisory conditions).

Finally, the Proposed Note addresses various procedural aspects of proposed Rule of Practice 194, including the following:

- In addition to the information required by the Proposed AP Rules, Disqualified AP Applications with respect to natural persons should be supplemented, where appropriate, by written statements of individuals who are competent to attest to the AP's character, employment performance and other relevant information (other than the applicant SBS Entity and the AP).
- In addition to the information required by the Proposed AP Rules, the SEC may request additional information to assist in its review of an application.

- Intentional misstatements or omissions of fact in the application may be criminal violations, and would make it less likely for the SEC to issue an SEC Order.
- The SEC will not consider any application that attempts to reargue or collaterally attack the findings that resulted in the statutory disqualification.

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Please do not hesitate to contact us with any questions.