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Part II

## Securities and Exchange Commission

17 CFR Part 240

Clearing Agency Standards for Operation and Governance; Proposed Rule

**SECURITIES AND EXCHANGE COMMISSION**

**17 CFR Part 240**

**[Release No. 34–64017; File No. S7–08–11]**

**RIN 3235–AL13**

## Clearing Agency Standards for Operation and Governance

**AGENCY:** Securities and Exchange Commission.

**ACTION:** Proposed rule.

**SUMMARY:** In accordance with Section 763 of Title VII ("Title VII") of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank Act"), Section 805 of Title VIII ("Title VIII") of the Dodd-Frank Act, and Section 17A of the Securities Exchange Act of 1934 ("Exchange Act"), the Securities and Exchange Commission ("SEC" or "Commission") is proposing rules regarding registration of clearing agencies and standards for the operation and governance of clearing agencies. The proposed rules are designed to enhance the regulatory framework for the supervision of clearing agencies.

**DATES:** Comments should be submitted on or before April 29, 2011.

**ADDRESSES:** Comments may be submitted by any of the following methods:

### Electronic Comments

- Use the Commission's Internet comment form (*http://www.sec.gov/rules/proposed.shtml*); or
- Send an e-mail to *rule-comments@sec.gov*. Please include File Number S7–8–11 on the subject line; or
- Use the Federal eRulemaking Portal (*http://www.regulations.gov*). Follow the instructions for submitting comments.

### Paper Comments

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F St., NE., Washington, DC 20549–1090.

All submissions should refer to File Number S7–8–11. This file number should be included on the subject line if e-mail is used. To help us process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (*http://www.sec.gov/rules/proposed.shtml*). Comments are also available for Web site viewing and printing in the Commission's Public Reference Room, 100 F St., NE., Washington, DC 20549 on official business days between the hours of 10 a.m. and 3 p.m. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

**FOR FURTHER INFORMATION CONTACT:** Jeffrey Mooney, Assistant Director; Peter Curley, Attorney Fellow; Andrew Blake, Special Counsel; Michael Milone, Special Counsel; Alison Duncan, Attorney-Adviser; Marta Chaffee, Branch Chief; and Andrew Bernstein, Attorney-Adviser, Office of Clearance and Settlement, Division of Trading and Markets, Securities and Exchange Commission, 100 F Street, NE., Washington, DC 20549–7010 at (202) 551–5710.

**SUPPLEMENTARY INFORMATION:** The Commission is proposing seven new rules and an amendment to an existing rule related to clearing agencies, including security-based swap clearing agencies. The proposed rules are designed to enhance the regulatory framework for the supervision of clearing agencies. Specifically, the Commission is proposing to: (1) Identify certain minimum standards for all clearing agencies; (2) require dissemination of pricing and valuation information by security-based swap clearing agencies that perform central counterparty services; (3) require all clearing agencies to have adequate safeguards and procedures to protect the confidentiality of trading information of clearing agency participants; (4) exempt certain security-based swap dealers and security-based swap execution facilities from the definition of a clearing agency; (5) amend rules concerning registration of clearing agencies to account for security-based swap clearing agencies and to make other technical changes; (6) require all clearing agencies to have procedures that identify and address conflicts of interest; (7) require standards for all members of clearing agency boards of directors or committees; and (8) require all clearing agencies to designate a chief compliance officer.

## I. Introduction

On July 21, 2010, President Barack Obama signed the Dodd-Frank Act into law.[1] The Dodd-Frank Act was enacted to, among other things, promote the financial stability of the United States by improving accountability and transparency in the financial system.[2] Title VII of the Dodd-Frank Act provides the Commission and the Commodity Futures Trading Commission ("CFTC") with the authority to regulate over-the-counter ("OTC") derivatives in light of the recent financial crisis, which demonstrated the need for enhanced regulation of the OTC derivatives market. The Dodd-Frank Act is intended to bolster the existing regulatory structure and to provide the Commission and the CFTC with effective regulatory tools to oversee the OTC derivatives market, which has grown exponentially in recent years and is capable of affecting significant sectors of the U.S. economy.[3]

The Dodd-Frank Act provides that the CFTC will regulate "swaps," the Commission will regulate "security-based swaps," and the CFTC and the Commission will jointly regulate "mixed swaps."[4] The Dodd-Frank Act amends the Exchange Act to require, among other things, the following: (1) Transactions in security-based swaps must be cleared through a clearing agency if they are of a type that the Commission determines must be cleared, unless an exemption from mandatory clearing applies; (2) transactions in security-based swaps must be reported to a registered security-based swap data repository or the Commission; and (3) if a security-

[1] The Dodd-Frank Wall Street Reform and Consumer Protection Act, Public Law 111–203, 124 Stat. 1376 (2010).

[2] *Id.* at Preamble.

[3] *See* 156 Cong. Rec. 5878 (daily ed. July 15, 2010) (statement of Sen. Dodd).

[4] The Commission and the CFTC, in consultation with the Board of Governors of the Federal Reserve System ("Federal Reserve"), shall jointly further define the terms "swap," "security-based swap," "swap dealer," "security-based swap dealer," "major swap participant," "major security-based swap participant," "eligible contract participant," and "security-based swap agreement." Public Law 111–203 § 712(d). Except for the term "eligible contract participant", these terms are defined in Sections 721 and 761 of the Dodd-Frank Act. Public Law 111–203 §§ 721, 761. The term "eligible contract participant," is defined in Section 1a(18) of the Commodity Exchange Act ("CEA"), 7 U.S.C. 1a(18), as re-designated and amended by Section 721 of the Dodd-Frank Act. Public Law 111–203 § 721. Further, Sections 721(c) and 761(b) of the Dodd-Frank Act respectively require the CFTC to adopt rules to further define the terms "swap," "swap dealer," "major swap participant," and "eligible contract participant," and permit the Commission to adopt rules to further define the terms "security-based swap," "security-based swap dealer," "major security-based swap participant," and "eligible contract participant," with regard to security-based swaps, for the purpose of including transactions and entities that have been structured to evade Title VII of the Dodd-Frank Act. Public Law 111–203 §§ 721(c), 761(b). Finally, Section 712(a) of the Dodd-Frank Act provides that the Commission and CFTC, after consultation with the Federal Reserve, shall jointly prescribe regulations regarding "mixed swaps," as may be necessary to carry out the purposes of Title VII. Public Law 111–203 § 712(a). Consistent with the Dodd-Frank statutory structure described above, the Commission and CFTC have proposed rules to define these terms. *See* Exchange Act No. 63452 (December 7, 2010), 75 FR 80174 (December 21, 2010).

based swap is subject to a clearing requirement, it must be traded on a registered trading platform, *i.e.,* a security-based swap execution facility or exchange, unless no facility makes such security-based swap available for trading.[5]

Beginning in December of 2008, the Commission acted to facilitate the clearing of OTC security-based swaps by permitting certain clearing agencies to clear credit default swaps ("CDS") on a temporary conditional basis.[6] Consequently, a significant volume of security-based swaps in the form of CDS transactions are centrally cleared today, and the Commission oversees those activities pursuant to the CDS Clearing Exemption Orders.[7]

## II. Prescribed Rulemaking for Clearing Agencies

### *A. Title VII of Dodd-Frank Act*

Title VII of the Dodd-Frank Act added new provisions to the Exchange Act that require clearing agencies that clear security-based swaps ("security-based swap clearing agencies") to register with the Commission[8] and require the Commission to adopt rules with respect to security-based swap clearing agencies.[9]

Specifically, new Section 17A(j) of the Exchange Act requires the Commission to adopt rules governing security-based swap clearing agencies.[10] New Section 17A(i) of the Exchange Act also gives the Commission authority to promulgate rules that establish standards for security-based swap clearing agencies.[11] Compliance with any such rules is a prerequisite to the registration of a clearing agency with the Commission and is also a condition to the maintenance of that security-based swap clearing agency's continued registration.[12]

### *B. Payment, Clearing, and Settlement Supervision Act of 2010*

Title VIII of the Dodd-Frank Act, entitled the Payment, Clearing, and Settlement Supervision Act of 2010 ("Clearing Supervision Act"), establishes an enhanced supervisory and risk control system for systemically important clearing agencies and other financial market utilities ("FMUs").[13] It provides that the Commission may prescribe regulations containing risk management standards, taking into consideration relevant international standards and existing prudential requirements, for any designated clearing entities it regulates.[14] The Council has not to date made any designations with respect to whether any FMU is, or is likely to become, systemically important;[15] however, the

[5] Section 761 of the Dodd-Frank Act adds Section 3(a)(77) to the Exchange Act, which defines the term "security-based swap execution facility" to mean "a trading system or platform in which multiple participants have the ability to execute or trade security-based swaps by accepting bids and offers made by multiple participants in the facility or system, through any means of interstate commerce, including any trading facility that (A) facilitates the execution of security-based swaps between persons; and (B) is not a national securities exchange." *See* Public Law 111–203 § 761. The decision of a security-based swap execution facility or exchange to list a security-based swap contract for trading may not be sufficient to establish that the contract is "made available for trading" by that security-based swap execution facility or exchange and therefore cannot be traded in the over-the-counter market. *See* Exchange Act Release No. 63825 (February 2, 2011), 76 FR 10948 (February 28, 2011). The Dodd-Frank Act amends the CEA to provide for a similar regulatory framework with respect to transactions in swaps regulated by the CFTC.

[6] The Commission authorized five entities to clear credit default swaps. *See* Exchange Act Release Nos. 60372 (July 23, 2009), 74 FR 37748 (July 29, 2009), 61973 (April 23, 2010), 75 FR 22656 (April 29, 2010) and 63389 (November 29, 2010), 75 FR 75520 (December 3, 2010) (CDS clearing by ICE Clear Europe Limited); 60373 (July 23, 2009), 74 FR 37740 (July 29, 2009), 61975 (April 23, 2010), 75 FR 22641 (April 29, 2010) and 63390 (November 29, 2010), 75 FR 75518 (December 3, 2010), (CDS clearing by Eurex Clearing AG); 59578 (March 13, 2009), 74 FR 11781 (March 19, 2009), 61164 (December 14, 2009), 74 FR 67258 (December 18, 2009), 61803 (March 30, 2010), 75 FR 17181 (April 5, 2010) and 63388 (November 29, 2010), 75 FR 75522 (December 3, 2010) (CDS clearing by Chicago Mercantile Exchange Inc.); 59527 (March 6, 2009), 74 FR 10791 (March 12, 2009), 61119 (December 4, 2009), 74 FR 65554 (December 10, 2009), 61662 (March 5, 2010), 75 FR 11589 (March 11, 2010) and 63387 (November 29, 2010) 75 FR 75502 (December 3, 2010) (CDS clearing by ICE Trust US LLC); 59164 (December 24, 2008), 74 FR 139 (January 2, 2009) (temporary CDS clearing by LIFFE A&M and LCH.Clearnet Ltd.) (collectively, "CDS Clearing Exemption Orders"). LIFFE A&M and LCH.Clearnet Ltd. allowed their order to lapse without seeking renewal.

[7] Most cleared CDS transactions have cleared at ICE Trust US LLC ("ICE Trust") or ICE Clear Europe Limited ("ICE Clear Europe"). However, Eurex Clearing AG ("Eurex") and the Chicago Mercantile Exchange Inc. ("CME") are also authorized to operate pursuant to the CDS Clearing Exemption Orders. As of October 8, 2010, ICE Trust had cleared approximately $7.1 trillion notional amount of CDS contracts based on indices of securities and approximately $490 billion notional amount of CDS contracts based on individual reference entities or securities. As of October 8, 2010, ICE Clear Europe had cleared approximately €3.09 trillion notional amount of CDS contracts based on indices of securities and approximately €560 billion notional amount of CDS contracts based on individual reference entities or securities. *See https://www.theice.com/marketdata/reports/ReportCenter.shtml.* The Commission has obtained data from The Depository Trust and Clearing Corporation on new and assigned CDS trades in United States Dollars during the month of November 2010 for ICE Trust. Cleared CDS trades represented a small fraction of total trades. Specifically, cleared trades were 5.24% by notional amount of all new or assigned single name trades, and 20.69% by notional amount of all new or assigned index trades.

[8] Public Law 111–203 § 763(b) (adding subparagraph (g) to Section 17A of the Exchange Act. Pursuant to Section 774 of the Dodd-Frank Act, the requirement in Section 17A(g) of the Exchange Act for securities-based swap clearing agencies to be registered with the Commission takes effect on July 16, 2011).

[9] Public Law 111–203 § 763(b) (adding subparagraphs (i) and (j) to Section 17A of the Exchange Act).

[10] Public Law 111–203 § 763(b) (adding subparagraph (j) to Section 17A of the Exchange Act). *See also* Public Law 111–203 § 774 of the Dodd-Frank Act (requiring that the provisions of Title VII take effect on the later of 360 days after the date of the enactment or, to the extent a provision of Title VII requires a rulemaking, not less than 60 days after publication of the final rule or regulation implementing such provision).

[11] Public Law 111–203 § 763(b) (adding subparagraph (i) to Section 17A of the Exchange Act).

[12] Under the Exchange Act, a clearing agency can be registered with the Commission only if the Commission makes a determination that the clearing agency satisfies the requirements set forth in paragraphs (A) through (I) of Section 17A(b)(3) of the Exchange Act.

[13] *See supra* note 1. Under Section 803 of the Clearing Supervision Act, clearing agencies may be FMUs. Therefore, the Commission may be the Supervisory Agency of a clearing agency that is designated as systemically important ("designated clearing entities") by the Financial Stability Oversight Council ("Council"). *See* 12 U.S.C. 5463. The definition of "FMU," which is contained in Section 803(6) of the Clearing Supervision Act, contains a number of exclusions including, but not limited to, designated contract markets, registered futures associations, swap data repositories, swap execution facilities, national securities exchanges, national securities associations, alternative trading systems, security-based swap data repositories, security-based swap execution facilities, brokers, dealers, transfer agents, investment companies and futures commission merchants. 12 U.S.C. 5462(6)(B). The designation of systemic importance hinges on a determination by the Council that the failure of, or a disruption to, the functioning of the FMU could create, or increase, the risk of significant liquidity or credit problems spreading among financial institutions or markets and thereby threaten the stability of the financial system of the United States. *See* 12 U.S.C. 5463(a)(2)(A)–(E). The designation of an FMU is significant, in part, because it will subject such designated entity to heightened oversight consistent with the terms of the Clearing Supervision Act. For example, the Clearing Supervision Act requires the Supervisory Agency to examine at least once annually any FMU that the Council has designated as systemically important. The Commission intends to conduct such annual statutory cycle examinations on the Commission's fiscal year basis. The Commission staff anticipates conducting the first annual statutory cycle examination of any designated FMU for which it is the Supervisory Agency in the annual cycle following such designation.

[14] *See* Section 805(a)(2) of the Clearing Supervision Act. Those regulations may govern "(A) the operations related to payment, clearing, and settlement activities of such designated clearing entities; and (B) the conduct of designated activities by such financial institutions." 12 U.S.C. 5464(a)(2).

[15] *See* 12 U.S.C 5321 (among other things establishing the Council and designating its voting and nonvoting members. In accordance with Section 804 of the Clearing Supervision Act, the Council has the authority, on a non-delegable basis and by a vote of not fewer than two-thirds of the members then serving, including the affirmative vote of its chairperson, to designate those FMUs that the Council determines are, or are likely to become, systemically important. The Council may,

Continued

Commission believes it is beneficial to consider the requirements of the Clearing Supervision Act in its proposed rules for clearing agencies because the Clearing Supervision Act may apply to one or more clearing agencies in the future and the Commission preliminarily believes that its goals are consistent with the goals of Section 17A of the Exchange Act. Specifically, Congress recognized in the Clearing Supervision Act that the operation of multilateral payment, clearing or settlement activities may reduce risks for clearing participants and the broader financial system, while at the same time creating new risks that require multilateral payment, clearing or settlement activities to be well-designed and operated in a safe and sound manner.[16] The Clearing Supervision Act is designed, in part, to provide a regulatory framework to help deal with such risk management issues, which is generally consistent with the Exchange Act requirement that clearing agencies be organized in a manner so as to facilitate prompt and accurate clearance and settlement, safeguard securities and funds and protect investors.[17]

*C. Section 17A of Exchange Act*

As noted above, in addition to the new authority provided to the Commission under Titles VII and VIII of the Dodd-Frank Act, the Commission has existing authority over clearing agencies under the Exchange Act. For example, entities are required to register with the Commission pursuant to Section 17A of the Exchange Act[18] and Rule 17Ab2–1,[19] prior to performing the functions of a clearing agency. Under this registration system, the Commission is not permitted to grant registration unless it determines that the rules and operations of the clearing agency meet the standards set forth in Section 17A.[20] If a clearing agency is granted registration, the Commission oversees the clearing agency to facilitate compliance with the Exchange Act through the rule filing process for self-regulatory organizations ("SROs") and through on-site examinations by Commission staff. Section 17A also gives the Commission authority to adopt rules for clearing agencies as necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Exchange Act and prohibits a registered clearing agency from engaging in any activity in contravention of these rules and regulations.[21]

## III. Proposed Rules Governing Clearing Agencies

The Commission is proposing several new rules that would set standards for the operation and governance of clearing agencies. As noted above, the Dodd-Frank Act specifically gives the Commission authority to regulate security-based swaps[22] and to adopt regulations addressing risk management standards for designated clearing entities that the Commission regulates. In addition to considering this specific directive in formulating the proposed rules, the Commission preliminarily believes that applying certain rules to all clearing agencies would promote financial stability, one of the goals of the Dodd-Frank Act, by facilitating prompt and accurate clearance and settlement of all securities transactions consistent with Section 17A of the Exchange Act while promoting the Dodd-Frank Act's stated aims of accountability and transparency.

The types of clearing agencies that are subject to the proposed rules can be divided into four different categories: (i) Clearing agencies that offer central counterparty ("CCP") services for transactions in securities that are not security-based swaps, (ii) clearing agencies that offer CCP services for transactions in securities that are security-based swaps; (iii) clearing agencies that provide non-CCP services for transactions in securities that are not security-based swaps; and (iv) clearing agencies that provide non-CCP services for transactions in securities that are security-based swaps. The table below illustrates how the proposed rules would apply to different types of clearing agencies. In general, as illustrated in column "A" in the table, clearing agencies offering CCP services (regardless of whether they offer those services for transactions in securities that are or are not security-based swaps) would be subject to most of the proposed rules.[23] Clearing agencies that offer only non-CCP services would only be subject to certain of the proposed rules, depending on whether they offer those services for transactions in securities that are not security-based swaps (as illustrated in column "B" in the table)[24] or that are security-based swaps (as illustrated in column "C" in the table).

APPLICATION OF PROPOSED RULES TO CLEARING AGENCIES

| | *A* CCP Clearing Services for Securities that are or are not Security-Based Swaps ("SBS") | *B* Non-CCP Clearing Services in Securities that are not SBS | *C* Non-CCP Clearing Services for Securities that are SBS |
|---|---|---|---|
| 17Ad–22(b)(1): Measurement and management of credit exposures | ○ | | |
| 17Ad–22(b)(2): Margin requirements | ○ | | |
| 17Ad–22(b)(3): Financial resources | ○ | | |
| 17Ad–22(b)(4): Model validation | ○ | | |

using the same procedures as discussed above, rescind such designation if it determines that the FMU no longer meets the standards for systemic importance. Before making either determination, the Council is required to consult with the Federal Reserve and the relevant Supervisory Agency as determined in accordance with Section 803(8) of the Clearing Supervision Act). *See also* Section 804 setting forth the procedures for giving entities 30 days advance notice and the opportunity for a hearing prior to being designated as systemically important. 12 U.S.C. 5463.

[16] 12 U.S.C. 5461(a)(2).

[17] *See* 15 U.S.C. 78q–1(b)(3)(A).

[18] *See* 15 U.S.C. 78q–1(b). *See also* Public Law 111–203 § 763(b) (adding subparagraph (g) to Section 17 of the Exchange Act).

[19] *See* 17 CFR 240.17b2–1.

[20] Specifically, Sections 17A(b)(3)(A)–(I) identify determinations that the Commission must make about the rules and structure of a clearing agency prior to granting registration. *See* 15 U.S.C. 78q–1(b)(3)(A)–(I). The staff of the Commission provided guidance on meeting the requirements of Section 17A in its Announcement of Standards for the Registration of Clearing Agencies. *See* Exchange Act Release No. 16900 (June 17, 1980), 45 FR 41920 (June 23, 1980).

[21] *See* 15 U.S.C. 78q–1(d).

[22] *See supra* note 4.

[23] As noted in the table, proposed Rule 17Aj–1 would only apply to CCPs for security-based swap transactions.

[24] Within this category, as illustrated in column "B", the proposed rules distinguish between clearing agencies that provide central securities depository services, and those that do not.

APPLICATION OF PROPOSED RULES TO CLEARING AGENCIES—Continued

| | *A* CCP Clearing Services for Securities that are or are not Security-Based Swaps ("SBS") | *B* Non-CCP Clearing Services in Securities that are not SBS | *C* Non-CCP Clearing Services for Securities that are SBS |
|---|---|---|---|
| 17Ad–22(b)(5): Non-dealer access | ○ | | |
| 17Ad–22(b)(6): Portfolio size and transaction volume thresholds restrictions | ○ | | |
| 17Ad–22(b)(7): Net capital restrictions | ○ | | |
| 17Ad–22(c)(1): Records of financial resources | ○ | | |
| 17Ad–22(c)(2): Audited financial statements | ○ | ○ | ○ |
| 17Ad–22(d)(1): Transparent and enforceable rules | ○ | ○ | ○ |
| 17Ad–22(d)(2): Participation requirements | ○ | ○ | ○ |
| 17Ad–22(d)(3): Custody of assets and investment risk | ○ | ○ | ○ |
| 17Ad–22(d)(4): Identification and mitigation of operational risk | ○ | ○ | ○ |
| 17Ad–22(d)(5): Money settlement risks | ○ | ○ | ○ |
| 17Ad–22(d)(6): Cost-effectiveness | ○ | ○ | ○ |
| 17Ad–22(d)(7): Links | ○ | ○ | ○ |
| 17Ad–22(d)(8): Governance | ○ | ○ | ○ |
| 17Ad–22(d)(9): Information on services | ○ | ○ | ○ |
| 17Ad–22(d)(10): Immobilization and dematerialization of stock certificates | | Would Only Apply to Clearing Agencies that Provide Central Securities Depository ("CSD") Services | |
| 17Ad–22(d)(11): Default procedures | ○ | ○ | ○ |
| 17Ad–22(d)(12): Timing of settlement finality | ○ | ○ | |
| 17Ad–22(d)(13): Delivery versus payment | ○ | ○ | |
| 17Ad–22(d)(14): Controls to address participants' failure to settle | | Would Only Apply to Clearing Agencies that Provide CSD Services | |
| 17Ad–22(d)(15): Physical delivery risks | ○ | ○ | |
| 17Aj–1: Dissemination of pricing and valuation information | Would Only Apply to Clearing Agencies that Provide CCP Services for SBS | | |
| 17Ad–23: Policies and procedures to protect confidentiality of trading information of participants | ○ | ○ | ○ |
| Amendments to Rule 17Ab2–1: Registration of clearing agencies | ○ | ○ | ○ |
| 17Ad–25: Procedures to identify and address conflicts of interests | ○ | ○ | ○ |
| 17Ad–26: Standards for board or board committee directors | ○ | ○ | ○ |
| 3Cj–1: Designation of chief compliance officer | ○ | ○ | ○ |

*A. Proposed Rule 17Ad–22 Standards for All Clearing Agencies*

The Commission is proposing Rule 17Ad–22 to augment the statutory requirements under the Exchange Act by establishing minimum requirements regarding how clearing agencies must maintain effective risk management procedures and controls as well as meet the statutory requirements under the Exchange Act on an ongoing basis. For a clearing agency to be registered under Section 17A, it must have the ability to facilitate the prompt and accurate clearance and settlement of transactions, safeguard investor funds and securities, remove impediments to and perfect the mechanism of a national clearance and settlement system, and generally protect investors.[25] Also, the clearing agency's rules must provide adequate access to qualified participants, fair representation of shareholders and participants, equitable pricing, fair discipline of participants, and must not impose any undue burden on competition.[26] Section 17A of the Exchange Act explicitly provides the Commission with discretion to update the rules for clearing agencies consistent with the Exchange Act.[27] Further, Section 805(a) of the Dodd-Frank Act directs the Commission to take into consideration relevant international standards and existing prudential requirements for clearing agencies that are designated as FMUs.[28] The current international standards most relevant to risk management of clearing agencies are the standards developed by the Technical Committee of the International Organization of Securities Commissions ("IOSCO") and the Committee on Payment and Settlement Systems ("CPSS") of the Bank for International Settlements that are contained in the following reports: *Recommendations for Securities Settlement Systems* (2001) ("RSSS"), and *Recommendations for Central Counterparties* (2004) ("RCCP") (collectively "CPSS–IOSCO Recommendations").[29]

The Commission preliminarily believes that certain aspects of the CPSS–IOSCO Recommendations should be made to clearly apply to clearing agencies and that such application would further the objectives and principles for clearing agencies under the Exchange Act and the Dodd-Frank Act, including those that are related to sound risk management practices and to fair and open access. These international standards were formulated by securities regulators and central banks to promote sound risk-management practices and encourage the safe design and operation of entities that provide clearance and settlement services. The Commission is proposing Rule 17Ad–22 (which is consistent with the CPSS–IOSCO Recommendations but reflects modifications designed to tailor the proposed rule to the Exchange Act and the U.S. clearance and settlement system) because the Commission preliminarily believes that the rule would help to facilitate prompt and accurate clearance and settlement, safeguard securities and funds and protect investors.[30]

The Commission preliminarily believes that the adoption of proposed Rule 17Ad–22, which is based on the CPSS–IOSCO Recommendations, and the application of this rule to all clearing agencies would have several important benefits, including providing a robust framework for assessing and addressing the risks within clearing agencies. The Commission requests comment on proposed Rule 17Ad–22 and the consideration of the CPSS–IOSCO Recommendations in connection with the proposed rule. The Commission also requests comment on whether the proposed rules are properly tailored to assess and address the risks at clearing agencies and whether they are sufficiently clear to enable clearing agencies to reasonably determine whether they are in compliance with the rules or whether the Commission should provide additional guidance.[31]

The Commission notes that IOSCO and the CPSS are currently in the process of revising their existing sets of international standards.[32] This review is intended to strengthen and clarify the CPSS–IOSCO Recommendations, as well as the CPSS's existing standards for payment systems entitled: *Core Principles for Systemically Important Payment Systems.* The Commission may, as international standards evolve, consider additional modifications to its rules as the Commission determines is appropriate based on its own experience and the requirements under the Exchange Act.

Proposed Rule 17Ad–22 contains certain additional requirements that are not addressed or contemplated by international standards. For clearing agencies that perform CCP services, these additional requirements are found in the following proposed rules: (1) Rule 17Ad–22(b)(3), which would require heightened financial resources for clearing agencies that provide CCP services for securities that are security-based swaps; (2) Rule 17Ad–22(b)(5), which would prohibit membership restrictions based on dealer status; (3) Rule 17Ad–22(b)(6), which would prohibit membership restrictions based on minimum volume and transaction thresholds; (4) Rule 17Ad–22(b)(7), which would prohibit restrictions on clearing agency membership based on minimum net capital requirements of $50 million or more; and (5) Rule 17Ad–22(c)(1), which would require calculation and maintenance of records of the clearing agency's financial resources. [33]

In addition, the Commission is proposing additional rules for all clearing agencies (whether or not they offer CCP services) that are not addressed or contemplated by the international standards. These proposed rules would: (1) Require dissemination of pricing and valuation information by security-based swap clearing agencies that perform CCP services (Proposed Rule 17Aj–1); (2) require all clearing agencies to have adequate safeguards and procedures to protect the confidentiality of trading information of

[25] *See* 15 U.S.C. 78q–1.

[26] *See id.*

[27] *See id.*

[28] 12 U.S.C. 5464(a)(1).

[29] The complete RSSS and RCCP Reports are available on the Web site of the Bank for International Settlements at *http://www.bis.org/publ/cpss46.htm* and *http://www.bis.org/publ/cpss64.htm* respectively.

The RSSS and RCCP Reports were drafted by IOSCO and CPSS ("Task Force"). The Task Force consisted of securities regulators and central bankers from 19 countries (*i.e.,* Australia, Belgium, Brazil, China, Czech Republic, France, Germany, Hong Kong, India, Italy, Japan, Malaysia, Mexico, The Netherlands, Saudi Arabia, Singapore, Spain, England, and the United States) and the European Union. The U.S. representatives on the Task Force included staff from the Commission, the Federal Reserve, and the CFTC. The Federal Reserve has incorporated the RSSS and RCCP, as well as the Core Principles for Systemically Important Payment Systems, in its Federal Reserve Policy on Payment System Risk. The Federal Reserve applies these standards in its supervisory process and expects systemically important systems, as determined by the Federal Reserve and subject to its authority, will complete a self-assessment against the standards set forth in the policy. *See* Policy on Payment System Risk, 72 FR 2518 (January 12, 2007).

[30] *See* 15 U.S.C. 78q–1(d).

[31] Several clearing agencies have published their evaluations of their compliance with the CPSS–IOSCO Recommendations on their Web sites. *See http://www.dtcc.com/legal/compliance/assessments.php.* In addition, several clearing agencies, as part of requests for the CDS Clearing Exemption Orders, have represented to the Commission that they met the standards set forth in the RCCP. *See supra* note 6.

[32] In December 2009, IOSCO and CPSS began a comprehensive review of existing standards for FMUs, which includes the RSSS and RCCP. This review intends to strengthen and clarify the standards based on experience with the standards since their publication and specifically from lessons learned during the recent financial crisis.

[33] Proposed Rule 17Ad–22(c)(2) would apply to all clearing agencies and require them to post annual audited financial reports on their Web sites.

clearing agency participants (Proposed Rule 17Ad–23); (3) exempt certain security-based swap dealers and security-based swap execution facilities from the definition of a clearing agency (Proposed Rule 17Ad–24); (4) amend rules concerning registration of clearing agencies to account for security-based swap clearing agencies and to make other technical changes (Rule 17Ab2–1); (5) require all clearing agencies to have procedures that identify and address conflicts of interest (Proposed Rule 17A–25); (6) require clearing agencies to set standards for all members of their boards of directors or committees (Proposed Rule 17Ad–26); and (7) require all clearing agencies to designate a chief compliance officer (Proposed Rule 3Cj–1).

1. Proposed Rule 17Ad–22(a)

Proposed Rule 17Ad–22(a) contains five definitions. Proposed Rule 17Ad–22(a)(1) would define CCP as a clearing agency that interposes itself between counterparties to securities transactions to act functionally as the buyer to every seller and as the seller to every buyer. Proposed Rule 17Ad–22(a)(2) would define "central securities depository services" to mean services of a clearing agency that is a securities depository as described in Section 3(a)(23) of the Exchange Act.[34] Proposed Rule 17Ad–22(a)(3) would define "participant", for the limited purposes of proposed Rules 17Ad–22(b)(3) and 17Ad–22(d)(14), to mean that if a participant controls another participant, or is under common control with another participant, then the affiliated participants shall be collectively deemed to be a single participant. Proposed Rule 17Ad–22(a)(4) would define "normal market conditions", for the limited purposes of proposed Rules 17Ad–22(b)(1) and (2), to mean conditions in which the expected movement of the price of cleared securities would produce changes in a clearing agency's exposures to its participants that would be expected to breach margin requirements or other risk control mechanisms only one percent of the time. Proposed Rule 17Ad–22(a)(5) would define "net capital", for the limited purposes of proposed Rule 17Ad–22(b)(7), to have the same meaning as set forth in Rule 15c3–1 under the Exchange Act for broker-dealers or any similar risk adjusted capital calculation for all other prospective clearing members.[35]

The Commission preliminarily believes that these five proposed definitions would be consistent with the common meaning of these terms as understood in the clearance and settlement industry. In addition, the Commission preliminarily believes the definition of "normal market conditions" would be consistent with international use of that term in the context of clearing agency risk management.[36] The Commission intends for these definitions to provide clearing agencies with appropriate guidance to determine when requirements under proposed Rule 17Ad–22 would apply. The Commission requests comment on the proposed definitions, including whether any additional clarification would be helpful.

2. Proposed Rule 17Ad–22(b)

Proposed Rule 17Ad–22(b) would set forth standards that are applicable to clearing agencies that provide CCP services. Specifically, the proposed rule would provide standards with respect to measurement and management of credit exposures, margin requirements, financial resources, and annual evaluations of the performance of the clearing agency's margin models. The proposed rule would also require membership access to clearing agencies for persons that are not dealers or security-based swap dealers, prohibit the use of minimum portfolio size and minimum volume transaction thresholds as a condition for membership at a clearing agency, and permit membership access to a clearing agency by persons with net capital equal to or greater than $50 million. The discussion below provides greater detail regarding each respective standard covered in proposed Rule 17Ad–22(b). The proposed rule is designed to address risks and participant membership structures that are specifically linked to the provision of services associated with a clearing agency interposing itself between counterparties to securities transactions and acting functionally as the buyer to every seller and the seller to every buyer (*i.e.,* CCP services). Accordingly, the Commission preliminarily believes that these requirements would not need to apply to clearing agencies that do not provide CCP services because they would not be engaged in activities that the proposed rule is designed to address.

The Commission preliminarily believes that proposed Rule 17Ad–22(b) would provide standards designed to help ensure sound risk management practices at clearing agencies providing CCP services. Further, the Commission preliminarily believes that the requirements of proposed Rule 17Ad–22(b) would help ensure that the rules, policies and procedures of a clearing agency providing CCP services will be designed to promote fair and open access, to promote the prompt and accurate clearance and settlement of securities transactions, and to assure the safeguarding of securities and funds that are in the custody or control of the clearing agency or for which it is responsible.

Proposed Rule 17Ad–22(b)(1): Measurement and Management of Credit Exposures

Proposed Rule 17Ad–22(b)(1) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to measure its credit exposures to its participants at least once each day, and limit its exposures to potential losses from defaults by its participants in normal market conditions[37] so that the operations of the clearing agency would not be disrupted and non-defaulting participants would not be exposed to losses that they cannot anticipate or control.

The Commission preliminarily believes that measurement and management of credit exposures can, among other things, reduce the likelihood in a participant default scenario that losses from default would disrupt the operations of the clearing agency and its non-defaulting participants and adversely affect the functioning of the clearing agency. A clearing agency providing CCP services faces the risk that its exposures to participants can change dramatically as a result of changes in prices, in positions, or both. Adverse price

[34] [Clearing agency] also means any person, such as a securities depository, who (i) acts as a custodian of securities in connection with a system for the central handling of securities whereby all securities of a particular class or series of any issuer deposited within the system are treated as fungible and may be transferred, loaned, or pledged by bookkeeping entry without physical delivery of securities certificates, or (ii) otherwise permits or facilitates the settlement of securities transactions or the hypothecation or lending of securities without physical delivery of securities certificates. 15 U.S.C. 78c(a)(23).

[35] As appropriate, the clearing agency would develop risk adjusted capital calculations for prospective clearing members that are not broker-dealers.

[36] In the context of the RCCP, "normal market conditions" means conditions in which the expected movement of the price of cleared securities would produce changes in a clearing agency's exposures to its participants that would be expected to breach margin requirements or other risk control mechanisms only one percent of the time. *See* CPSS Publications *Recommendations for Central Counterparties,* (November 2004), *available at http://www.bis.org/publ/cpss64.htm.*

[37] *See supra* note 36.

movements can rapidly increase exposures to participants, and participants may rapidly change or concentrate their positions through new trading. If not appropriately measured and managed, such results could lead to significant liabilities accruing at the clearing agency.

Recognizing that the risks that clearing agencies are likely to face will change over time, the Commission is proposing that a clearing agency providing CCP services be required to measure its credit exposures to its participants at least once each day. The Commission preliminarily believes this is the minimum frequency of measurement that would permit a clearing agency to effectively consider the risks it faces because of the potential for significant changes to the risk profiles of its participants to change on a daily basis.

In addition to requiring clearing agencies to take steps to measure their credit exposures to participants, the proposed rule would also require clearing agencies to limit their exposures to potential losses from participant defaults. By collecting sufficient margin and having other resources in place to account for losses arising under normal market conditions, the Commission expects that a clearing agency would be able to limit its exposures to potential losses from defaults by its participants. The Commission preliminarily believes that the proposed rule should thereby help ensure prompt and accurate clearance and settlement.

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(b)(1). In addition, the Commission requests comments on the following specific issues:

- Is the Commission's proposed rule regarding measurement and management of credit exposures sufficiently clear? If not, why not and what would be a better alternative?
- How do current practices of clearing agencies providing CCP services with respect to measurement and management of credit exposures compare to the practices that the Commission proposes to require in this rule? What are the expected incremental costs to clearing agencies providing CCP services in connection with adding to or revising their current practices in order to implement the Commission's proposed rule?
- Should the Commission require clearing agencies acting as CCPs to use any specific confidence level for limiting potential losses under the proposed rule when clearing certain products, or to use minimum amounts of market data when calculating credit exposures? Why or why not?
- What level of discretion should the Commission allow clearing agencies providing CCP services to exercise when measuring and managing credit exposure? Are there circumstances when such discretion should be limited?
- Is it more difficult for clearing agencies providing CCP services and their participants to anticipate and control losses associated with certain types of financial products compared to others? If so, how should the Commission take this into account when establishing rules for clearing agency standards? For example, should the Commission require additional risk management measures to be applied by clearing agencies providing CCP services when judging the risks associated with financial products that trade infrequently or when valuation models for the product are not yet broadly accepted in the financial market? Why or why not?
- Extremely illiquid security-based swap products may be difficult to clear under a conventional CCP clearing model because it may be difficult to value them with a degree of accuracy that allows the CCP to properly manage the risk of those positions. Should the Commission explore developing alternatives to the requirements contained in proposed Rule 17Ad–22(b)(1) based on the liquidity of products a clearing agency clears? What effect would any such requirements have on the potential development of alternative clearing models for highly-illiquid products that would convey some of the benefits of clearing (such as centralized holding of collateral by a third-party custodian, daily adjustment of variation margin amounts, daily posting and return of variation margin, independent valuation of positions, and prompt close-out of positions held by a defaulting market participant)?
- Should the Commission consider requiring clearing agencies that provide CCP services to measure exposures to participants more or less frequently than a minimum of once daily?

Proposed Rule 17Ad–22(b)(2): Margin Requirements

Proposed Rule 17Ad–22(b)(2) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to: (i) Use margin requirements to limit its credit exposures to participants in normal market conditions; [38] (ii) use risk-based models and parameters to set margin requirements; and (iii) review the models and parameters at least monthly.

The Commission preliminarily believes that use of margin requirements by clearing agencies providing CCP services to collect assets (*e.g.,* cash or securities) from its participants as a way to limit exposures to participants in normal market conditions would, among other things, provide the clearing agency with assets it could readily use to limit losses incurred by a participant in the event of a default. By limiting its credit exposure in this manner, a clearing agency providing CCP services would be less likely to be subject to disruptions in its operations as a result of a participant default, thereby promoting prompt and accurate clearance and settlement.

The Commission also preliminarily believes that risk-based models and parameters should be used to set margin requirements because they permit a clearing agency providing CCP services to tailor the amount of margin collected to the needs of the clearing agency. Specifically, models and parameters for collecting margin that account for the risks the clearing agency providing CCP services faces when transacting with a participant may be more likely to result in effective and efficient margin requirements because the level of margin collected would be commensurate with the level of risk presented by the participant to the clearing agency.

In addition, the Commission preliminarily believes that the review of these models and parameters should be required to occur at least monthly. Market conditions and risks are constantly changing and therefore the models and parameters used by a clearing agency providing CCP services to set margin may not accurately reflect the needs of a clearing agency if they are permitted to remain static. The Commission recognizes, however, that there may be benefits to maintaining some stability with respect to margin levels in order to limit operational difficulties. Accordingly, the Commission is proposing that clearing agencies providing CCP services be required to review their models and parameters at least monthly because the Commission preliminarily believes that such time frame would limit the potential that such parameters or models will become stale while also providing the clearing agency flexibility to maintain some stability with respect

[38] *See supra* note 36.

to determinations for margin requirements.

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(b)(2). In addition, the Commission requests comments on the following specific issues:

- Is the Commission's proposed rule regarding margin requirements sufficiently clear? If not, why not and what would be a better alternative?
- How do current practices of clearing agencies regarding margin requirements compare to the practices that the Commission proposes to require in this rule? What are the expected incremental costs to clearing agencies in connection with adding to or revising their current practices in order to implement the Commission's proposed rule?
- Should the Commission require clearing agencies providing CCP services to impose any special margin or intraday margin requirements in certain circumstances? Are there circumstances when special margin or intraday margining would not be appropriate? Why or why not?
- Should the Commission allow clearing agencies providing CCP services to exercise significant discretion when establishing margin practices? Why or why not? Are there circumstances when such discretion should be limited? Is there a risk that clearing agencies providing CCP services may lower margin standards to compete for business? If so, how should the Commission take such factors into account when establishing rules for clearing agencies providing CCP services?
- Should the Commission consider requiring a clearing agency that provides CCP services to review its margin model and parameters more or less frequently than at least monthly?

Proposed Rule 17Ad–22(b)(3): Financial Resources

Proposed Rule 17Ad–22(b)(3) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to maintain sufficient financial resources to withstand, at a minimum, a default by the participant to which it has the largest exposure in extreme but plausible market conditions, provided that a security-based swap clearing agency shall maintain sufficient financial resources to withstand, at a minimum, a default by the two participants to which it has the largest exposures in extreme but plausible market conditions.[39]

The Commission preliminarily believes that requiring a clearing agency, other than a security-based swap clearing agency, that provides CCP services to maintain sufficient financial resources to withstand, at a minimum, a default by the participant to which it has the largest exposure in extreme but plausible market conditions would, among other things, reduce the likelihood that a default would create losses that would disrupt the operations of the clearing agency and adversely affect the clearing agency's non-defaulting participants. However, the Commission preliminarily believes that security-based swap clearing agencies that provide CCP services face additional risk-management challenges because of factors unique to the security-based swaps market, such as more limited historical information on pricing and the jump-to-default risk[40] associated with certain security-based swaps, such as CDS. The Commission preliminarily believes that to promote prompt and accurate clearance and settlement and maintain higher levels of financial resources to account for these risks, it is important for security-based swap clearing agencies that provide CCP services to be able to withstand a default by the two participants to which the clearing agency has its largest exposures in extreme but plausible market conditions. Moreover, the Commission expects that when a clearing agency that provides CCP services determines what level of financial resources would be sufficient to account for exposures in extreme but plausible market conditions, the clearing agency would consider potential losses that would be greater than those resulting from observed periods of significant volatility or disturbances.

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(b)(3). In addition, the Commission requests comments on the following specific issues:

- Is the Commission's proposed rule regarding requiring clearing agencies providing CCP services to maintain sufficient financial resources sufficiently clear? If not, why not and what would be a better alternative?
- Should the Commission require all clearing agencies providing CCP services, instead of only those clearing security-based swaps, to maintain sufficient financial resources to withstand a default by the two participants to which it has the largest exposures in extreme but plausible market conditions? Should all or any subset of clearing agencies be required to maintain sufficient financial resources based on more or less than two participant defaults? For example, should the financial resources requirements be different for certain clearing agencies, such as security-based swap clearing agencies or those designated as systemically important under the Clearing Supervision Act? Should the Commission require that financial resources be measured based on a different standard than resources needed to withstand default by a certain number of participants, such as a percentage of the total business conducted by the clearing agency?
- How do current practices of clearing agencies pertaining to financial resources compare to the practices that the Commission proposes to require in this rule? What are the expected incremental costs to clearing agencies in connection with adding to or revising their current practices in order to implement the Commission's proposed rule?
- Are the financial resources standards for clearing agencies providing CCP services proposed by the Commission sufficient for the proper functioning of a clearing agency? Should a clearing agency providing CCP services be able to mutualize losses during a default using financial resources designed to cover price movements? Should the Commission establish more specific rules? For example, should the Commission establish standards for the level of clearing agency resources maintained in a guarantee fund as opposed to a margin fund, or should clearing agencies providing CCP services be given discretion to manage the composition of their financial resources as they see fit? Why or why not? Should the Commission establish more prescriptive requirements concerning the financial resources of certain clearing agencies providing CCP services, such as those

[39] *See* proposed Rule 17Ad–22(a)(3), *supra* Section II.A.1 (defining "participant" for purposes of proposed Rule 17Ad–22(b)(3)).

[40] Jump-to-default risk relates to the possibility of a reference entity unexpectedly experiencing a credit event over a short period resulting in significant changes in the value of any CDS contracts written on that particular reference entity. For example, a seller of a CDS could be collecting regular premiums with little expectation that the reference entity may default. However, if that reference entity suddenly experiences a credit event, it will trigger an unexpected obligation on the protection seller to pay a lump sum, dependent on the size of the contract, to the protection buyer. *See generally* Darrell Duffie and Haoxiang Zhu, *Does a Central Clearing Counterparty Reduce Counterparty Risk?* (Stanford Univ. 2010), *available at http://www.stanford.edu/~duffie/DuffieZhu.pdf.*

that clear security-based swaps or those that are designated as systemically important under the Clearing Supervision Act?

• Should the Commission provide additional guidance regarding what constitutes "extreme but plausible market conditions"? Does allowing clearing agencies providing CCP services discretion to interpret this term create uncertainty or introduce more risk into the financial system than might otherwise be the case?

• What are clearing agencies' providing CCP services and their participants' incentives to maintain financial resources to withstand the foreseeable consequences of participant defaults? Are there identifiable circumstances in which these self-interested incentives may vary? For example, do clearing agencies providing CCP services with public shareholders have different incentives than clearing agencies providing CCP services that are member-owned? Can the capital structure of the clearing agency providing CCP services and the order in which losses are suffered by defaulting parties, surviving participants and any public shareholders affect the level of risk accepted by the clearing agency? If so, how should the Commission take these factors into account when establishing rules for clearing agencies providing CCP services?

Proposed Rule 17Ad–22(b)(4): Model Validation

Proposed Rule 17Ad–22(b)(4) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide for an annual model validation process consisting of evaluating the performance of the clearing agency's margin models and the related parameters and assumptions associated with such models by a qualified person who does not perform functions associated with the clearing agency's margin models (except as part of the annual model validation) and does not report to a person who performs these functions.[41]

The Commission preliminarily believes that clearing agencies that provide CCP services need to have a qualified person conduct a review of models that are used to set margin levels, along with related parameters and assumptions, in order to assure that the models perform in a manner that facilitates prompt and accurate clearance and settlement of transactions. In determining whether a person is qualified to conduct the model validation, clearing agencies providing CCP services could consider several factors, including the person's experience in validating margin models, expertise in risk management generally, and understanding of the clearing agency's operations and procedures.

In addition, the Commission is proposing that the person conducting the model validation be a person who does not perform functions associated with the clearing agency's margin models (except as part of the annual model validation) and does not report to a person who performs these functions. The Commission preliminarily believes that a review by a person who is not involved in the day-to-day operation of the margin model is important to identify potential vulnerabilities or limitations and to promote a critical evaluation of the model. This is because a person involved in the functions related to the model's operation, or someone who reports to such a person, may be less likely to critically evaluate the margin model because of preconceived views or a desire not to find issues with a model that they help to operate.[42] The Commission preliminarily believes that the person validating the clearing agency's margin model should be sufficiently free from outside influences so that he or she can be completely candid in their assessment of the model.

Finally, the Commission is proposing that the model validation be conducted on an annual basis. The Commission preliminarily believes that conducting the model validation on an annual basis would provide a sufficiently frequent evaluation period because model performance ordinarily would not be expected to vary significantly over short periods but should be re-evaluated as market conditions change.

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(b)(4). In addition, the Commission requests comments on the following specific issues:

• Is the Commission's proposed rule requiring clearing agencies to provide for a model validation sufficiently clear? If not, why not and what would be a better alternative?

• What are the advantages and disadvantages of requiring an annual model validation? Should a more or less frequent model validation be required? Should the model validation be specifically triggered as a result of any material change in the clearing agency, such as the introduction of new products or the addition of portfolio margining arrangements with other clearing agencies?

• Should the Commission place more or less stringent restrictions on the type of person who is permitted to conduct the model validation? For example, should the Commission prescribe any specific qualifications that the person conducting the model validation should have? Should the Commission require an outside consultant be engaged to conduct the model validation? Should persons that perform functions associated with the clearing agency's margin model be able to conduct the model validation?

• Does the proposal provide sufficient or excessive separation of the person conducting the model validation from the persons who develop and administer the model? In either case, please explain. Should the Commission adopt additional requirements to help ensure that the persons conducting the model validation are free from retaliation and influence? If so, please explain. What costs or burdens might such additional requirements impose on the effective validation of models?

Proposed Rule 17Ad–22(b)(5): Non-Dealer Member Access

Proposed Rule 17Ad–22(b)(5) requires a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide the opportunity for a person that does not perform any dealer[43] or security-based swap dealer[44] services to

[41] Any person responsible for supervising the operation of the clearing agency's margin model would be viewed as performing the functions associated with the clearing agency's margin model and could not therefore have supervisory authority over the person conducting the model validation.

[42] Proposed Rule 17Ad–22(b)(4), however, would not prevent a person conducting the model validation from being employed by the clearing agency if the conditions in the proposed rule are satisfied. For example, a qualified member of the internal audit function that operates under a separate reporting line may be able to provide the model validation.

[43] The term "dealer" is defined in Section 3(a)(5) of the Exchange Act and means any person engaged in the business of buying and selling securities for such person's own account through a broker or otherwise. The definition contains an exception for a person that buys or sells securities for such person's own account, either individually or in a fiduciary capacity, but not as a part of a regular business. There is also an exception for banks engaging in certain specified activities. *See* 15 U.S.C. 78c(a)(5) for the complete definition.

[44] Pursuant to Section 761 of the Dodd-Frank Act, the term "security-based swap dealer" is added as Section 3(a)(71) of the Exchange Act, 15 U.S.C. 78c(a), and generally means any person who (A) holds itself out as a dealer in security-based swaps; (B) makes a market in security-based swaps; (C) regularly enters into security-based swaps with counterparties as an ordinary course of business for

obtain membership on fair and reasonable terms at the clearing agency in order to clear securities for itself or on behalf of other persons. Dealer and security-based swap dealer services generally involve services designed to facilitate securities transactions by buying and selling securities for a person's own account. The Commission preliminarily believes that requiring clearing agencies that perform CCP services to allow persons who are not dealers or security-based swap dealers to become members of the clearing agency will promote more competition in and access to clearing through facilitating indirect clearing arrangements, commonly referred to as correspondent clearing. Correspondent clearing is an arrangement between a current participant of a clearing agency and a non-participant that desires to use the clearing agency for clearance and settlement services.

The Commission has previously noted that in situations where direct access to clearing agencies is limited by reasonable participation standards firms that do not meet these standards may still be able to access clearing agencies through correspondent clearing arrangements with direct participants.[45] Such a process would involve the non-participant entering into a correspondent clearing arrangement with a participant so that the transaction may be submitted by the participant to the clearing agency. Thus, the success of correspondent clearing arrangements depends on the willingness of participants to enter into such arrangements with non-participant firms which may act as direct competitors to the participants in the participants' capacity as dealers or security-based swap dealers in the market for buying or selling the relevant securities. Given that participants that are dealers or security-based swap dealers may have an incentive to restrict clearing access to potential competitors, correspondent clearing arrangements may not be readily established without providing participants that do not provide dealer or security-based swap dealer services with the ability to become members of a clearing agency and thereby help develop correspondent clearing arrangements.

At the same time, the Commission recognizes that persons who are not dealers or security-based swap dealers may fail to meet other standards for membership at a clearing agency, such as the operational capabilities required for direct participation. Proposed Rule 17Ad–22(b)(5) would not prohibit clearing agencies that provide CCP services from taking these factors into account when establishing membership criteria for non-dealers. Rather, the proposal would prohibit clearing agencies that provide CCP services from denying membership on fair and reasonable terms to otherwise qualified persons solely by virtue of the fact that they do not perform any dealer or security-based swap dealer services.

The Commission preliminarily believes that the incentives of persons who do not provide dealer or security-based swap dealer services to promote access at the clearing agency that provides CCP services would not be limited by a desire to restrict competition in the market for buying or selling the relevant securities. Accordingly, the Commission preliminarily believes that permitting such persons to become members of a clearing agency that provides CCP services may foster the development of correspondent clearing arrangements that would allow dealers and security-based swap dealers, who may otherwise not be able to meet reasonable participation standards of a clearing agency, to obtain access to the clearing agency through correspondent clearing arrangements. The Commission preliminarily believes this would be beneficial because it could result in greater competition in and access to clearing.

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(b)(5). In addition, the Commission requests comments on the following specific issues:

- In addition to prohibiting denial of membership based on whether a person provides dealer or security-based swap dealer services as a way to facilitate greater indirect access to clearing, should the Commission consider other measures to promote access to clearing at clearing agencies that provide CCP services, including any requirements designed to promote greater direct access to clearing (*e.g.,* adding specific membership categories)?
- Should clearing agencies that provide CCP services be required to have policies and procedures that are designed to promote membership by non-dealers? If so, what would be the advantages and disadvantages of requiring the clearing agency to periodically measure its performance against the objectives contained in such policies and procedures, and who within the clearing agency should be responsible for conducting such a review (for instance the chief compliance officer)?
- Is the Commission's proposed rule requiring clearing agencies that provide CCP services to provide the opportunity for a person that does not perform any dealer or security-based swap dealer services to obtain membership at the clearing agency to clear securities for itself or on behalf of other persons sufficiently clear? If not, why not?
- Should the Commission consider more prescriptive regulations to specify the criteria that clearing agencies should use to grant membership privileges to persons that do not perform any dealer or security-based swap dealer services to clear securities for themselves or on behalf of other persons? Please explain why or why not.
- What are the potential advantages and disadvantages of having persons that do not provide dealer or security-based swap dealer services as members of a clearing agency?
- If a clearing agency that provides CCP services does not have rules that facilitate correspondent clearing, should the Commission consider requiring that clearing agency to justify to the Commission why its rules do not facilitate correspondent clearing? What would be the advantages and disadvantages of such a requirement? What are the potential reasons why a clearing agency may not have rules that facilitate correspondent clearing arrangements?
- Should the Commission consider limiting the proposed requirement for providing membership access to persons who do not provide dealer or security-based swap dealer services to a certain category of clearing agencies, such as security-based swap clearing agencies that provide CCP services or those designated as systemically important? Please explain why or why not. In particular, are there special considerations, such as market concentration, affecting security-based swap clearing agencies that provide CCP services that make access to those clearing agencies for non-dealers particularly important? If not, why not? If so, what are those considerations and how would this requirement address

its own account; or (D) engages in any activity causing it to be commonly known in the trade as a dealer or market maker in security-based swaps. *See* Public Law 111–203, Section 761 for the complete definition. *See also* Exchange Act Release No. 63452 (December 7, 2010), 75 FR 80174 (December 21, 2010), *supra* note 4.

[45] *See* Exchange Act Release No. 63107 (October 14, 2010), 75 FR 65882 (October 26, 2010) (Ownership Limitations and Governance Requirements for Security-Based Swap Clearing Agencies, Security-Based Swap Execution Facilities, and National Securities Exchanges with Respect to Security-Based Swaps under Regulation MC).

them? Do any similar considerations exist, or is there a potential that similar considerations could exist in the future, with respect to clearing agencies that clear securities other than security-based swaps? Would there be any advantages or disadvantages to maintaining one standard for all clearing agencies that provide CCP services? Please explain.

Proposed Rule 17Ad–22(b)(6): Portfolio Size and Transaction Volume Thresholds Restrictions

Proposed Rule 17Ad–22(b)(6) prohibits a clearing agency that provides CCP services from having membership standards that require that participants maintain a portfolio of any minimum size or that participants maintain a minimum transaction volume. The Commission notes that the proposed rule would not prohibit a clearing agency that provides CCP services from considering portfolio size and transaction volume as one of several factors when reviewing a potential participant's operations. Rather, the proposed rule would prohibit the establishment of minimum portfolio sizes or transaction volumes that by themselves would act as barriers to participation by new participants in clearing. Such minimum thresholds would not function as a good indicator of whether a participant is able to meet its obligations to a clearing agency.[46] This is because new participants to a clearing agency that provides CCP services that do not initially intend to transact in substantial size or volume may nevertheless have the operational and financial capacity to perform the activities that other participants are able to perform. Therefore, the Commission preliminarily believes that the proposed rule may help to facilitate the requirement in Section 17A of the Exchange Act that the rules of a clearing agency permit fair and open access.[47]

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(b)(6). In addition, the Commission requests comments on the following specific issues:

- Is the Commission's proposed rule prohibiting clearing agencies that provide CCP services from having membership standards that require participants to maintain a portfolio of any minimum size or to meet a minimum transaction volume threshold sufficiently clear? If not, why not?
- What are the potential advantages and disadvantages of prohibiting clearing agency membership standards from requiring participants to maintain a minimum portfolio size or meet a minimum transaction volume threshold? Please explain.
- Should the Commission consider imposing the proposed requirements on all clearing agencies, rather than only those that provide CCP services? Why or why not?
- Should the Commission consider prohibiting only security-based swap clearing agencies that provide CCP services from having membership standards that require participants to maintain a minimum portfolio size or to maintain a minimum transaction volume? Please explain why or why not. In particular, are there special considerations affecting security-based swap clearing agencies that provide CCP services that make it particularly important to prevent use of these specific criteria in their membership standards? If so, what are those special considerations and how would this requirement address them? If not, in what ways would such a requirement impact the operations of security-based swap clearing agencies that provide CCP services and other types of clearing agencies? Would there be advantages to maintaining one standard for all clearing agencies that provide CCP services? Why or why not?

Proposed Rule 17Ad–22(b)(7): Net Capital Restrictions

Proposed Rule 17Ad–22(b)(7) requires a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide a person that maintains net capital[48] equal to or greater than $50 million with the opportunity to obtain membership at the clearing agency, with any net capital requirements being scalable so that they are proportional to the risks posed by the participant's activities to the clearing agency. This means that while a clearing agency that provides CCP services could not restrict access to the clearing agency solely because a participant does not have a net capital level above $50 million, the clearing agency's policies and procedures could be reasonably designed to limit the activities of the participant in comparison to the activities of other participants that maintained a higher net capital level. For example, as a way to help make its requirements scalable, a clearing agency may elect to place limits on its potential exposure to participants operating at certain net capital thresholds by restricting the maximum size of the portfolio such participants are permitted to maintain at the clearing agency. The Commission preliminarily believes that persons that maintain a net capital level of $50 million would have sufficient net capital to be able to participate at some level in a clearing agency that provides CCP services, provided that they are able to comply with other reasonable membership standards. Based on broker-dealer reporting data available to the Commission, the $50 million threshold for net capital is a standard that only approximately 4% of the total number of broker-dealers could satisfy. Accordingly, the Commission preliminarily believes that prohibitions on membership access that are based solely on persons having net capital equal to or greater than $50 million could introduce unnecessary barriers to clearing access. The Commission also preliminarily believes that the proposed rule would facilitate sound risk management practices by the clearing agencies by encouraging the clearing agencies to examine and articulate the benefits of higher net capital requirements as a result of having clearing agencies develop scalable membership standards that link the nature and degree of participation with the potential risks posed by the participant.[49]

Proposed Rule 17Ad–22(b)(7) also permits a clearing agency to provide for a higher net capital requirement (*i.e.,* higher than $50 million) as a condition for membership at the clearing agency if the clearing agency demonstrates to the Commission that such a requirement is necessary to mitigate risks that could not otherwise be effectively managed by other measures, such as scalable limitations on the transactions that the participants may clear through the clearing agency, and the Commission approves the higher net capital requirement as part of a rule filing or

[46] Proposed Rule 17Ad–22(b)(6) would not prohibit a clearing agency from imposing maximums portfolio sizes or transaction volume amounts.

[47] *See infra* note 59.

[48] Proposed Rule 17Ad–22(a)(5) would define "net capital", for the limited purposes of proposed Rule 17Ad–22(b)(7), to have the same meaning as set forth in Rule 15c3–1 under the Exchange Act for broker-dealers or any similar risk adjusted capital calculation for all of other prospective clearing members.

[49] The Commission notes there are examples of capital-related requirements that differentiate among types of participants. For instance, the Fixed Income Clearing Corporation has maintained a $50 million net worth requirement and $10 million excess net capital requirement for its Category 1 Dealer Netting Members and a $25 million net worth requirement and $10 million excess net capital requirement for its Category 2 Dealer Netting Members.

clearing agency registration application. The Commission preliminarily believes that by providing a method for clearing agencies to impose higher net capital requirements in circumstances where such requirements are necessary to mitigate risks, the proposed rule would provide appropriate flexibility for risk management purposes.

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(b)(7). In addition, the Commission requests comments on the following specific issues:

- Is the Commission's proposed rule limiting the ability of clearing agencies that provide CCP services to deny membership access to participants with $50 million or more in net capital sufficiently clear? If not, why not?
- What are advantages or disadvantages of requiring a clearing agency that provides CCP services to provide a person that maintains a net capital equal to or greater than $50 million with the ability to obtain membership at the clearing agency, with any net capital requirements being scalable so that they are proportional to the risks posed by the participant's activities to the clearing agency?
- Should the Commission consider a higher or lower threshold for net capital than the proposed $50 million amount? Please explain and describe the rationale for the desired threshold amount.
- Should the Commission consider providing for the adjustment of the $50 million net capital threshold to reflect inflation, deflation or other factors? If so, how should the Commission make such adjustment?
- Would access to clearing agencies that provide CCP services by dealers or security-based swap dealers that are not currently members of such clearing agencies be significantly improved as a result of the proposed requirement?
- Are there any difficulties that clearing agencies that provide CCP services may encounter in implementing a system that seeks to scale net capital to the risk that a participant brings to a clearing agency? Would clearing agencies be able to effectively model such risks to prevent the potential of significant losses above the amounts of margin collected? How would clearing agencies seek to limit the activities of participants to prevent the risk of significant losses above the amounts of margin collected?
- Does the proposal, to permit a clearing agency to provide for a higher net capital requirement (*i.e.,* higher than $50 million) as a condition for membership at the clearing agency if the clearing agency demonstrates to the Commission that such a requirement is necessary to mitigate risks that could not otherwise be effectively managed by other measures, provide sufficient flexibility to be able to address potential risk management concerns? Would the proposal lead to higher or lower levels of risk at clearing agencies? Please explain.
- Should the Commission consider requiring only security-based swap clearing agencies that provide CCP services to be subject to this requirement? Please explain why or why not. In particular, are there special considerations affecting security-based swap clearing agencies that provide CCP services, such as market concentration, that make it particularly important for a person that maintains net capital equal to or greater than $50 million to have the ability to obtain membership? If so, what are those special considerations and how would this requirement address them? If not, in what ways would this requirement impact the operations of security-based swap clearing agencies that provide CCP services and other clearing agencies? Would there be any advantages or disadvantages to maintaining one requirement for all clearing agencies that provide CCP services? Please explain.

3. Proposed Rule 17Ad–22(c)

Proposed Rule 17Ad–22(c)(1) would provide that each fiscal quarter (based on calculations made as of the last business day of the clearing agency's fiscal quarter), or at any time upon Commission request, a clearing agency that performs central counterparty services shall calculate and maintain a record [50] of the financial resources necessary to meet its requirement in proposed Rule 17Ad–22(b)(3) and sufficient documentation to explain the methodology it uses to compute such financial resource requirement.

The Commission preliminarily believes that it would be appropriate to require clearing agencies that provide CCP services to make these calculations quarterly or at any time based on the request of the Commission because this proposed requirement would provide a periodic update of the financial resources that are needed as market conditions change, while also providing flexibility for the Commission to request such calculations on a real-time basis, which may be useful during periods of market stress or other circumstances where more timely information is desired. These calculations and related documentation should help the Commission in its oversight of clearing agencies' compliance with proposed Rule 17Ad–22(b)(3) by providing a clear record of the method used by the clearing agency providing CCP services to maintain sufficient financial resources.

Proposed Rule 17Ad–22(c)(2) would require a clearing agency to post on its Web site an annual audited financial report. Each financial report would be required to (i) be a complete set of financial statements of the clearing agency for the most recent two fiscal years of the clearing agency and be prepared in accordance with U.S. generally accepted accounting principles ("U.S. GAAP"), except that for a clearing agency that is a corporation or other organization incorporated or organized under the laws of any foreign country, the financial statements may be prepared according to U.S. GAAP or International Financial Reporting Standards as issued by the International Accounting Standards Board ("IFRS"); (ii) be audited in accordance with standards of the Public Company Accounting Oversight Board by a registered public accounting firm that is qualified and independent in accordance with Rule 2–01 of Regulation S–X (17 CFR 210.2–01); and (iii) include a report of the registered public accounting firm that complies with paragraphs (a) through (d) of Rule 2–02 of Regulation S–X (17 CFR 210.2–02). The Commission preliminarily believes that requiring the posting of the clearing agency's audited annual financial report would provide an additional layer of information about the activities and financial strength of the clearing agency that market participants may find useful in assessing their use of the clearing agency's services.[51]

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(c). In addition, the Commission requests comments on the following specific issues:

- Is the Commission's proposed rule regarding calculating and maintaining a record of the financial resources necessary pursuant to proposed Rule 17Ad–22(b)(3) sufficiently clear? If not,

[50] *See* Exchange Act Rule 17a–1 (17 CFR 240.17a–1). Clearing agencies may destroy or otherwise dispose of records at the end of five years consistent with Exchange Act Rule 17a–6 (17 CFR 240.17a–6).

[51] The requirements of proposed Rule 17Ad–22(c)(2) concerning the audited annual financial report would apply individually to each respective clearing agency.

why not and what would be a better alternative?

• How do current practices by clearing agencies providing CCP services compare to the practices that the Commission proposes requiring in this rule with respect to determining needed financial resources? What are the expected incremental costs to clearing agencies that provide CCP services in connection with adding to or revising their current practices in order to implement the Commission's proposed rule?

• Should the Commission require calculation of the financial resources related information more or less frequently than quarterly? Why or why not?

• Should the Commission require any other financial statements of a clearing agency to be posted on its Web site, such as quarterly financial statements?

• What are the advantages and disadvantages of permitting a financial report to be in compliance with IFRS as an alternative to U.S. GAAP? If the Commission adopts the proposal to permit certain clearing agencies to report using IFRS as published by the IASB, should the Commission require a reconciliation to U.S. GAAP for specified accounts? If so, what accounts or items would be most useful to participants and other regulators? Would permitting only clearing agencies that are incorporated or organized under the laws of any foreign country to report under IFRS create any incentives for changing jurisdictions of incorporation or organization? If it is permitted, should we exclude certain clearing agencies, such as those who fall within one or more of the following categories: (i) Those whose financial reports have not been audited by an independent public accountant inspected by the PCAOB, (ii) those who have not received a "clean" audit opinion, or (iii) those who have previously had to correct a material error in their financial statements?

4. Proposed Rule 17Ad–22(d)

Proposed Rule 17Ad–22(d) would set forth certain standards that relate to clearance and settlement processes. The areas addressed include: (1) Transparent and enforceable rules and procedures; (2) participation requirements; (3) custody of assets and investment risk; (4) operational risk; (5) money settlement risk; (6) cost-effectiveness; (7) links; (8) governance; (9) information on services; (10) immobilization and dematerialization of stock certificates; (11) default procedures; (12) timing of settlement finality; (13) delivery versus payment; (14) risk controls to address participants' failures to settle; and (15) physical delivery risks. The discussion below provides greater detail regarding each respective standard covered in proposed Rule 17Ad–22(d).

Proposed Rule 17Ad–22(d)(1): Transparent and Enforceable Rules and Procedures

Proposed Rule 17Ad–22(d)(1) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide for a well founded, transparent and enforceable (legally and practically) structure for each aspect of their activities in all relevant jurisdictions.[52] The clearing agency should have written policies and procedures[53] in place that, at a minimum, address the significant aspects of a clearing agency's operations and risk management in order to provide a well founded legal framework and must be clear, internally consistent, and readily accessible by the public in order to provide a transparent legal framework. In addition, the clearing agency must be able to enforce its policies and procedures that contemplate enforcement by the clearing agency. Moreover, policies and procedures that govern or create remedial measures that a party other than the clearing agency (such as a clearing member) can undertake to seek redress or to promote compliance with applicable rules must be enforceable.[54] For the clearing agency's policies and procedures to be enforceable, a clearing agency must have appropriate means to compel parties to comply in a timely manner, including members or service providers of clearing agencies that are non-U.S. persons. The Commission preliminarily believes this proposed requirement would help to reduce the legal risks involved in the clearance and settlement process. Such legal risks include, among other things, the likelihood that the policies and procedures of a clearing agency are incomplete, opaque, or not enforceable and will therefore adversely affect the functioning of the clearing agency.[55] Because they would function to reduce these legal risks, the Commission preliminarily believes that well founded, transparent and enforceable policies and procedures established by the clearing agency to underpin the clearing agency's operational and business activities are essential to a clearing agency's ability to facilitate the prompt and accurate clearance and settlement of securities transactions and safeguard securities and funds as required for the protection of investors by Section 17A of the Exchange Act.[56]

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(d)(1). In addition, the Commission requests comments on the following specific issues:

• Is the Commission's proposed rule regarding policies and procedures providing for a well founded, transparent, and enforceable legal framework sufficiently clear? If not, why not? Is there a better alternative?

• How would this proposal affect the current practices of clearing agencies in formulating policies and procedures? Would the proposed rule affect the costs of providing clearing agency services? Please explain.

• What are the advantages and disadvantages of taking into account that legal risks may vary by the types of services offered by clearing agencies and whether the clearing agency operates in multiple jurisdictions? Are there any considerations, such as issues concerning compliance with regulations under various jurisdictions, that the Commission should take into account for clearing agencies operating in multiple jurisdictions?

• Should the Commission consider more prescriptive rules to define how clearing agencies would provide for a well founded, transparent and enforceable legal framework? Please explain why or why not. Alternatively, should the Commission consider more prescriptive rules that would apply in the context of approval of a clearing agency's application for registration?

• Should the Commission require a clearing agency to submit legal opinions or other supporting evidence to demonstrate the legal adequacy of the mechanisms at the clearing agency that

[52] A relevant jurisdiction would include, among others, activities (i) in the United States, (ii) involving any means of interstate commerce, or (iii) in respect to providing clearing services to any U.S. person. For clearing agencies that operate in multiple jurisdictions, this also could include resolving possible conflicts of laws issues that the clearing agency may encounter.

[53] Clearing agencies are SROs as defined in Section 3(a)(26) of the Exchange Act. A stated policy, practice, or interpretation of an SRO, such as a clearing agency's written policies and procedures, would generally be deemed to be a proposed rule change. *See* 17 CFR 240.19b–4.

[54] The Commission preliminarily believes that proposed Rule 17Ad–22(d)(1) would augment the Exchange Act requirement that the rules of the clearing agency must provide that its participants shall be appropriately disciplined for any violation of any provision of the rules of the clearing agency. *See* 15 U.S.C. 78q–1(b)(3)(G).

[55] *See generally*, RSSS Recommendation 1, Legal Framework and RCCP Recommendation 1, Legal Risk.

[56] 15 U.S.C. 78q–1(a)(1)(A).

are in place to handle participant defaults?

Proposed Rule 17Ad–22(d)(2): Participation Requirements

Proposed Rule 17Ad–22(d)(2) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to require participants to have sufficient financial resources and robust operational capacity to meet obligations arising from participation in the clearing agency. This proposed requirement is intended to reduce the likelihood of defaults by participants, while also providing flexibility to tailor standards that are linked to the obligations of the participant. As a result, the Commission preliminarily believes this requirement would protect investors and facilitate prompt and accurate clearance and settlement by promoting membership standards at clearing agencies that are likely to limit the potential for defaults.

The proposed rule also would require clearing agencies to have procedures in place to monitor that participation requirements are met on an ongoing basis. Operational and financial stability of participants is subject to market forces and can therefore change over time. Because participants collectively contribute to the operational and financial stability of a clearing agency, the Commission preliminarily believes that the proposed requirement to continue to monitor compliance with the clearing agency's participation requirements supports the Exchange Act requirement that clearing agencies are able to facilitate prompt and accurate clearance and settlement.[57]

In addition, clearing agencies would be required to have participation requirements that are objective,[58] publicly disclosed, and facilitate fair and open access.[59] The Commission preliminarily believes this requirement would foster compliance with the requirement under Section 17A of the Exchange Act that the rules of a clearing agency must not be designed to permit unfair discrimination in the admission of participants by requiring standards that are designed to be measurable, open and fair.[60]

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(d)(2). In addition, the Commission requests comments on the following specific issues:

- Is the Commission's proposed rule regarding participation requirements sufficiently clear? If not, why not and what would be a better alternative?
- How do current practices of registered clearing agencies with respect to participation standards compare to the proposed requirements in this rule? Are there any expected costs or benefits to clearing agencies in connection with adding to or revising their participation standards in order to implement this portion of the Commission's proposed rule?
- Should the Commission's proposed rule regarding participation requirements be more specific? If so, why and in what way? Should the Commission's proposed rule regarding participation requirements be less specific to allow for greater flexibility? If so, why and in what way?
- Should more specific monitoring obligations be imposed to ensure compliance with participation standards? For example, should the Commission consider mandating an independent review of the process for monitoring participants' compliance with the clearing agency's participation requirements? Why or why not?

Proposed Rule 17Ad–22(d)(3): Custody of Assets and Investment Risk

Proposed Rule 17Ad–22(d)(3) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to hold assets in a manner whereby risk of loss or of delay in access to them is minimized. Minimizing the risk of loss or delay in access is intended to refer to holding assets in ways that, to the extent reasonably practicable, would limit the potential for loss of those assets and delay in access to them. For example, the Commission is aware that clearing agencies currently seek to minimize the risk of loss or delay in access by holding assets that are highly-liquid (*e.g.,* cash, U.S. Treasury securities or securities issued by a U.S. government agency) and engaging banks to custody the assets and facilitate settlement. Compliance with the proposed requirement is intended to improve the ability of the clearing agency to meet its settlement obligations by reducing the likelihood that assets securing participant obligations to the clearing agency would be unavailable or insufficient when the clearing agency needs to draw on them. The proposed rule would also require clearing agencies to invest assets in instruments with minimal credit, market, and liquidity risks. A requirement that a clearing agency hold assets in instruments with minimal credit, market and liquidity risk may promote the clearing agency's ability to retrieve these assets promptly. That, in turn, could help to increase the potential for a clearing agency to timely meet its settlement obligations to its participants.

The Commission preliminarily believes that proposed Rule 17Ad–22(d)(3) would strengthen the requirement in Section 17A(b)(3)(F) of the Exchange Act that the rules of a clearing agency must be designed to ensure the safeguarding of securities and funds in the custody or control of the clearing agency or for which the clearing agency is responsible.[61] In this way, the Commission preliminarily believes the proposed rule would also promote protection of the financial market served by the clearing agency.

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(d)(3). In addition, the Commission requests comments on the following specific issues:

- Are the proposed rule's requirements regarding custody and investment of assets sufficiently clear? If not, why not and what would be a better alternative?
- How do current practices of clearing agencies for holding or investing in assets compare to the Commission's proposal? What are the expected incremental costs to clearing agencies in connection with adding to or revising these current practices in order to comply with the Commission's proposed rule?
- Are there any other factors not mentioned that the Commission should take into consideration with respect to

[57] 15 U.S.C 78q–1(b)(3)(A).

[58] Objective criteria would generally include, but not be limited to, criteria that are based on measureable facts such as capital requirements.

[59] Having open access, in part, involves having a process for admission of participants that does not unfairly discriminate. *See* 15 U.S.C. 78q–1(b)(3)(F) ("The rules of a clearing agency * * * are not designed to permit unfair discrimination in the admission of participants or among participants in the use of the clearing agency"). In addition, the Dodd-Frank Act added Section 3C to the Exchange Act which provides in relevant part: "(2) OPEN ACCESS.—The rules of a clearing agency described in paragraph (1) shall— (A) prescribe that all security-based swaps submitted to the clearing agency with the same terms and conditions are economically equivalent within the clearing agency and may be offset with each other within the clearing agency; and (B) provide for non-discriminatory clearing of a security-based swap executed bilaterally or on or through the rules of an unaffiliated national securities exchange or security-based swap execution facility." Public Law 111–203 § 763(a) (adding Section 3C to the Exchange Act).

[60] 15 U.S.C. 78q–1(b)(3)(F).

[61] 15 U.S.C. 78q–1(b)(3)(F).

minimizing custody of assets and investment risk?

• Should clearing agencies ever be permitted to hold assets in instruments that do not have minimal credit, market and liquidity risk? If so, why and under what circumstances?

• What measures should clearing agencies have in place to minimize risk of loss or delay in access to assets? Should the proposed rule specify any such measures?

Proposed Rule 17Ad–22(d)(4): Identification and Mitigation of Operational Risk

Proposed Rule 17Ad–22(d)(4) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to identify sources of operational risk and minimize these risks through the development of appropriate systems, controls, and procedures. A clearing agency that develops systems, controls and procedures which, taken as a whole, are designed to limit the identified sources of operational risk to the extent reasonably practicable would be able to satisfy this requirement. The proposed rule also would require clearing agencies to implement systems that are reliable, resilient and secure and have adequate scalable capacity. This should help to ensure that clearing agencies are able to operate with minimal disruptions, even during times of market stress when there may be greater demands on their systems due to higher volume. In addition, the proposed rule would require that clearing agencies have business continuity plans that allow for timely recovery of operations and ensure the fulfillment of a clearing agency's obligations. This requirement would be relevant in the event of, among other things, deficiencies in information systems or internal controls, human errors, management failures, unauthorized intrusions into corporate or production systems, or disruptions from external events such as natural disasters.

The Commission preliminarily believes that the requirements under proposed Rule 17Ad–22(d)(4) should collectively help to address risks posed by potential operational deficiencies to the clearing agency and its participants. Specifically, to help limit disruptions that may impede the proper functioning of a clearing agency, the Commission preliminarily believes it is imperative that clearing agencies review their operations for potential weaknesses and develop appropriate systems, controls, and procedures to address weaknesses contemplated under the proposed rule. Moreover, the Commission preliminarily believes that maintaining reliable, resilient and secure systems with adequate backup capability, as well as continuity plans providing for timely recovery of operations, are essential components of facilitating prompt and accurate clearance and settlement. The Commission intends for proposed Rule 17Ad–22(d)(4) to complement the existing guidance provided by the Commission in its Automation Review Policy statements[62] and Interagency White Paper on Sound Practices to Strengthen the Resilience of the U.S. Financial System.[63]

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(d)(4). In addition, the Commission requests comments on the following specific issues:

• Is the Commission's proposed rule regarding identification and mitigation of operational risk sufficiently clear? If not, why not and what would be a better alternative?

• How do current practices of clearing agencies with respect to operational risks compare to the practices that the Commission proposes to require in this rule? What are the expected incremental costs to clearing agencies in connection with adding to or revising their current practices relating to operational risks in order to implement the Commission's proposed rule?

• Should the Commission's proposal require a specific methodology to identify and mitigate operational risk? If so, what is the methodology and why should this methodology be required?

• Should the Commission require that business continuity plans be tested with participants on an ongoing basis or with a specified frequency? Should any other more prescriptive requirements be considered by the Commission?

• Would a clearing agency's ability to comply with the proposed rule be affected if the clearing agency's operations were outsourced to another firm? If so, how should the proposed rule address these differences in compliance? Would the need to minimize operational risk require limits on the types of operations that can be outsourced by clearing agencies? Would the answer depend on whether the function was outsourced to an affiliated or unaffiliated firm? Please explain.

Proposed Rule 17Ad–22(d)(5): Money Settlement Risks

Proposed Rule 17Ad–22(d)(5) would require clearing agencies establish, implement, maintain and enforce written policies and procedures reasonably designed to employ money settlement arrangements that eliminate or strictly limit the clearing agency's settlement bank risks, that is, its credit and liquidity risks from the use of banks to effect money settlements with its participants, and require funds transfers to the clearing agency to be final when effected. The Commission notes that there are a number of arrangements that clearing agencies could establish to comply with the proposed rule. For example, a clearing agency could establish criteria for use of banks to effect money settlements with its participants that address the banks' creditworthiness, access to liquidity, and operational reliability. Where practicable, a clearing agency could use multiple settlement banks and monitor the concentration of payments among its settlement banks. A clearing agency also could employ agreements with such banks to ensure that funds transfers to the clearing agency are final when effected. In addition, where available, a clearing agency could use a central bank to effect money settlements with its participants. Use of the Federal Reserve System in the United States or other central bank would eliminate the risks associated with using a settlement bank.[64]

These proposed requirements are meant to reduce the risk that financial obligations related to the activities of a clearing agency are not timely settled or discharged with finality. Failure by a bank to effectuate timely and final settlement adversely affects the clearing

[62] *See* Exchange Act Release Nos. 27445 (November 16, 1989), 54 FR 48704 ("ARP I") and 29815 (May 9, 1991), 56 FR 22489 ("ARP II"). Generally, the guidance in ARP I and ARP II provides for the following activities by clearing agencies: (1) Performing periodic risk assessments of its automated data processing ("ADP") systems and facilities; (2) providing for the selection of the clearing agency's independent auditors by non-management directors and authorizing such non-management directors to review the nature, scope, and results of all audit work performed; (3) having an adequately staffed and competent internal audit department; (4) furnishing annually to participants audited financial statements and an opinion from an independent public accountant as to the clearing agency's system of internal control—including unaudited quarterly financial statements also should be provided to participants upon request; and (5) developing and maintaining plans to assure the safeguarding of securities and funds, the integrity of the ADP system, and recovery of securities, funds, or data under a variety of loss or destruction scenarios.

[63] *See* Exchange Act Release No. 47638 (April 7, 2003), 68 FR 17809 (April 11, 2003), *available at http://www.sec.gov/news/studies/34-47638.htm.*

[64] The Board of Governors of the Federal Reserve System will determine whether systemically important clearing agencies may obtain account access from the Federal Reserve System.

agency by exposing it to credit and liquidity pressures that can destabilize the clearing agency's ability to facilitate prompt and accurate clearance and settlement. Accordingly, the Commission is proposing this new rule, which is designed to limit the potential that the money settlement arrangements cause the clearing agency to face higher levels of credit and liquidity risks and to provide assurance that funds transfers are final when effected. In addition, the Commission preliminarily believes that the proposed rule would assist a clearing agency in meeting the requirement of Section 17A(b)(3)(F) of the Exchange Act, which requires the rules of a clearing agency to be designed to assure the safeguarding of securities and funds which are in the custody or control of the clearing agency or for which it is responsible.[65]

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(d)(5). In addition, the Commission requests comments on the following specific issues:

- Is the Commission's proposed rule regarding money settlement risk sufficiently clear? If not, why not and what would be a better alternative?
- How do current practices regarding money settlement risk of clearing agencies compare to the practices that the Commission proposes to require in this rule? What are the expected incremental costs to clearing agencies in connection with adding to or revising their current practices regarding money settlement risk in order to implement the Commission's proposed rule?
- Would it be reasonable to eliminate the clearing agency's credit and liquidity risks from the use of banks to effect money settlements with its participants? If so, how?
- Are there other rules that the Commission should establish regarding money settlement risk management, for example, by mandating the minimum number of banks that a clearing agency may use to effect money settlements with its participants in order to avoid reliance on a small number of such banks, or by specifying characteristics of financial institutions that may be used by clearing agencies for settlement purposes? If so, what would be the appropriate rules and what would be the effect of adopting them?
- Should rules for money settlement risk management established by the Commission be uniform, or are there circumstances in which it would be appropriate for clearing agencies to accept a higher level of money settlement risk, such as when transacting in certain product categories or with certain types of customers? Could the rules proposed by the Commission limit the ability of clearing agencies to compete for certain types of business either within the United States or internationally? Why or why not?
- Should the Commission adopt rules to govern the clearing agency's use of banks that are affiliated with participants in the clearing agency? Should the Commission prohibit this practice? Please explain.

Proposed Rule 17Ad–22(d)(6): Cost-Effectiveness

Proposed Rule 17Ad–22(d)(6) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide that their operations are cost-effective in meeting the requirements of participants while maintaining the safety and security of operations. To maintain safe and secure operations, a clearing agency would need to comply with the requirements under the Exchange Act and the rules thereunder. For example, a clearing agency would need to maintain the ability to comply with any recordkeeping or other regulatory requirement. Having clearing agencies be mindful of the costs that are incurred by their participants, while maintaining such compliance, should help to reduce inefficiencies in the provision of clearing agency services. This is particularly important in circumstances where clearing agencies may not be subject to strong competitive forces (such as when there is only one clearing agency for an asset class) for the provision of their services and therefore may have less of an incentive to be cost-effective in meeting the requirements of participants. Accordingly, the Commission preliminarily believes the proposed rule is appropriate in the public interest, for the protection of investors, because it would potentially help reduce the costs incurred for clearing agency services while also maintaining appropriate standards for a clearing agency's operations.

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(d)(6). In addition, the Commission requests comments on the following specific issues:

- Would the proposed rule help to assure that a clearing agency's operations are cost-effective? Does the proposed rule establish a standard for maintaining cost-effectiveness that is sufficiently clear? If not, why not and how might the rule be altered?
- Are there any other requirements that the Commission should include in the rule to help ensure that clearing agencies are cost-effective in providing clearing and settlement services while also maintaining safe and secure operations and compliance with all regulatory requirements?
- Does any specific business model for clearing agencies help to promote cost-effectiveness? Should the business model of a clearing agency affect the type of rule regarding cost-effectiveness that should apply to the clearing agency?
- Should the Commission consider issuing additional guidance on how clearing agencies could be cost-effective in meeting the requirements of participants while maintaining safe and secure operations? If so, what type of guidance would be helpful?

Proposed Rule 17Ad–22(d)(7): Links

Proposed Rule 17Ad–22(d)(7) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to evaluate the potential sources of risks that can arise when the clearing agency establishes links either cross-border or domestically to clear trades, and to ensure that these risks are managed prudently on an ongoing basis.

Section 17A(a)(1)(D) of the Exchange Act states that the linking of all clearance and settlement facilities and the development of uniform standards and procedures for clearance and settlement will reduce unnecessary costs and increase the protection of investors and persons facilitating transactions by and acting on behalf of investors.[66] Further, Section 17A(b)(3)(F) of the Exchange Act requires that the rules of a clearing agency foster cooperation and coordination with persons engaged in the clearance and settlement of securities transactions.[67] In the clearance and settlement process, links should help deepen market liquidity and enable participants to trade in other markets.[68] However, by tying the

[65] 15 U.S.C. 78q–1(b)(3)(F).

[66] 15 U.S.C. 78q–1(a)(1)(D).

[67] 15 U.S.C. 78q–1(b)(3)(F).

[68] For example, The Depository Trust Company's ("DTC") Canadian Link Service allows qualifying DTC participants to clear and settle valued securities transactions with participants of a Canadian securities depository. The link is designed to facilitate cross-border transactions by allowing participants to use a single depository interface for U.S. and Canadian dollar transactions and eliminate the need for split inventories. *See* Exchange Act Release Nos. 52784 (November 16,

Continued

clearing operations of different clearing agencies together, link arrangements potentially expose a clearing agency and its members to the risk management profile of another clearing organization and to the risk of financial loss if that clearing organization experiences a default or is otherwise unable to meet its settlement obligations.[69]

Although the design and operation of each link will present a unique risk profile, clearing agencies potentially face legal, operational, credit and liquidity risks from link arrangements. In addition, because links can create interdependencies, clearing agencies may be affected by systemic risk if there are deficiencies in these arrangements. The Commission preliminarily believes that requiring clearing agencies to evaluate and monitor any link arrangements they maintain is essential to protect the marketplaces that clearing agencies serve because the requirement would reduce the likelihood that such arrangements perpetuate risks that could create disruptions in the operations of clearing agencies. Accordingly, the Commission is proposing this rule, which would require clearing agencies to evaluate and manage the risks associated with its links.

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(d)(7). In addition, the Commission requests comments on the following specific issues:

- Is the Commission's proposed rule regarding evaluating link arrangements and prudently managing the associated risks on an ongoing basis sufficiently clear? If not, why not and how might the rule be stated more clearly?
- How do current practices of clearing agencies with respect to link arrangements meet or fail to meet the standard that the Commission proposes to require in this rule? What are the expected incremental costs to clearing agencies in connection with adding to or revising their current practices for link arrangements to comply with the Commission's proposed rule?
- Should the Commission include specific requirements regarding the clearing agency's responsibility to evaluate a link for, among other things, the other clearing organization's structure, financial strength, regulatory and disciplinary history, disaster recovery, banking relationships and lines of credit, and risk management controls?
- Should the Commission establish additional requirements for clearing agencies that create linkages with other parties, such as information reporting requirements to the Commission? Would such additional requirements reduce or increase the likelihood that linkages would be established in appropriate circumstances?
- How could clearing agencies ensure that the laws and contractual rules governing linked systems support the design of the link and provide adequate protection to both clearing agencies and their participants? Are additional rules or requirements needed when a link is established with a non-U.S. clearing organization?
- Should the Commission place any limits on or promote the use of linked arrangements in light of potential effects on systemic risk?

Proposed Rule 17Ad–22(d)(8): Governance

Proposed Rule 17Ad–22(d)(8) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent to fulfill the public interest requirements in Section 17A of Exchange Act applicable to clearing agencies,[70] to support the objectives of owners and participants, and to promote the effectiveness of the clearing agency's risk management procedures.[71]

Clear and transparent governance arrangements promote accountability and reliability in the decisions, rules and procedures of the clearing agency because they provide interested parties (such as owners, participants, and general members of the public) with information about how such decisions are made and what the rules and procedures are designed to accomplish.[72] The key components of a clearing agency's governance arrangements include the clearing agency's ownership structure, the composition and role of its board, the structure and role of board committees, reporting lines between management and the board, and the processes that ensure management is held accountable for the clearing agency's performance.

Governance arrangements have the potential to play an important role in making sure that clearing agencies fulfill the Exchange Act requirements that the rules of a clearing agency be designed to protect investors and the public interest and to support the objectives of owners and participants. Similarly, governance arrangements may promote the effectiveness of a clearing agency's risk management procedures by creating an oversight framework that fosters a focus on the critical role that risk management plays in promoting prompt and accurate clearance and settlement.[73]

The Commission preliminarily believes that the requirements regarding governance arrangements contained in proposed Rule 17Ad–22(d)(8) would be appropriate in the public interest and for the protection of investors because they would enhance the ability of a clearing agency to serve the interests of its various constituents and the interests of the general public while maintaining prudent risk management processes to promote prompt and accurate clearance and settlement.

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(d)(8). In addition, the Commission requests comments on the following specific issues:

- Is the Commission's proposed rule regarding clear and transparent governance arrangements sufficiently clear? If not, why not and how might the rule be stated more clearly?
- Would the proposed rule require clearing agencies to change their current

2005), 71 FR 70902 (November 23, 2005) and 55239 (February 5, 2007), 72 FR 6797 (February 13, 2007) (File No. SR–DTC 2006–15).

[69] A clearing agency may be required to enter into a participant agreement with the other clearing organization as part of the link arrangement, which includes sharing in the loss allocations of that clearing organization. *See* RCCP 4.10.6, *supra* note 29.

[70] Section 17A(b)(3)(F) of the Exchange Act requires that the rules of a clearing agency be designed to protect investors and the public interest. 15 U.S.C. 78q–1(b)(3)(F).

[71] Proposed Rule 17Ad–22(d)(8) would complement other applicable requirements concerning governance at clearing agencies that may also separately apply. These other requirements include the existing regulatory framework of Section 17A of the Exchange Act and the related requirements contemplated by proposed Rule 17Ad–25, as well as Section 765 of the Dodd-Frank Act with respect to security-based swap clearing agencies. *See supra* Section III.F. (proposing that clearing agencies be required to establish, implement, maintain and enforce written policies and procedures reasonably designed to identify and address existing or potential conflicts of interest). *See also* Exchange Act Release No. 63107, 75 FR 65882, *supra* note 45.

[72] The Exchange Act currently requires that certain aspects of a clearing agency's governance arrangements be made clear and transparent. Section 19(b) of the Exchange Act requires that clearing agencies, as SROs, file with the Commission any proposed rule or any proposed change in, addition to, or deletion from the rules of the clearing agency, accompanied by a concise general statement of the basis and purpose of the proposed rule change. 15 U.S.C. 78s(b).

[73] The role of governance arrangements in promoting effective risk management has also been a focus of rules recently proposed by the Commission to mitigate conflicts of interest at security-based swap clearing agencies. *See* Exchange Act Release No. 63107, 75 FR 65882, *supra* note 45.

practices with respect to governance arrangements? If so, how? What are the expected incremental costs to clearing agencies in connection with adding to or revising their current practices with respect to governance arrangements in order to implement the Commission's proposed rule?

• Are there any other requirements that should be included in the rule to promote clear and transparent governance arrangements, such as mandating specific board or ownership structures? If so, what should they be?

• Should the Commission propose more prescriptive requirements for the governance of all clearing agencies? If so, what should they be? For example, should the Commission specify certain reporting lines or board composition?

• How direct should the Commission's role be in the oversight and monitoring of the composition and activities of clearing agency boards and board committees? If the Commission's role should be more direct, what mechanisms or structure would facilitate the Commission taking such a role? For example, should the Commission consider any additional requirements related to fiduciary duties to either enhance mitigation of conflicts or address deficiencies?

Proposed Rule 17Ad–22(d)(9): Information on Services

Proposed Rule 17Ad–22(d)(9) would require clearing agencies establish, implement, maintain and enforce written policies and procedures reasonably designed to provide market participants with sufficient information for them to identify and evaluate the risks and costs associated with using clearing agencies' services. The types of information that a clearing agency may disclose, as appropriate, to its participants to satisfy this requirement include the clearing agency rulebook,[74] the costs of its services, a description of netting and settlement activities the clearing agency provides, procedures relating to participants' rights and obligations, information regarding the clearing agency's margin methodology, and information regarding the "extreme but plausible" scenarios that the clearing agency uses to stress test its financial resources. Requiring a clearing agency to disclose information sufficient for participants to identify risks and costs associated with using the clearing agency will allow participants to make informed decisions about the use of the clearing agency and take appropriate actions to mitigate their risks and costs associated with the use of the clearing agency. Accordingly, the Commission's proposed rule is designed to promote participants' understanding of the risks and costs associated with using a clearing agency's services, thereby facilitating prompt and accurate clearance and settlement, safeguarding securities and funds and protecting investors.[75]

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(d)(9). In addition, the Commission requests comments on the following specific issues:

• Is the Commission's proposed rule regarding providing market participants with sufficient information to identify and evaluate the risks and costs associated with using the clearing agency's services sufficiently clear? If not, why not and what would be a better alternative?

• How do current practices of clearing agencies with respect to providing market participants with information meet or fail to meet the requirements in the proposed rule? What are the expected incremental costs to clearing agencies in connection with adding to or revising their current practices in order to implement the proposed requirements?

• Should the Commission consider more detailed requirements concerning disclosure of certain matters such as pricing information and the cost of specific services, as well as default and risk management procedures? Why or why not?

• Should any of the examples of the types of information that a clearing agency may disclose be specifically required to be provided by clearing agencies to their participants or to the public?

Proposed Rule 17Ad–22(d)(10): Immobilization and Dematerialization of Stock Certificates

Proposed Rule 17Ad–22(d)(10) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to immobilize[76] and dematerialize[77] securities certificates and transfer them by book entry to the greatest extent possible when the clearing agency provides central securities depository services.[78] The Commission preliminarily believes that the immobilization and dematerialization of securities and their transfer by book entry would result in reduced costs and risks associated with securities settlements and custody by removing the need to hold and transfer many, if not most, physical certificates.[79] The Commission also preliminarily believes that the proposed rule would strengthen the requirement in Section 17A(b)(3)(F) of the Exchange Act that requires the rules of a clearing agency to assure the safeguarding of securities and funds that are in the custody or control of the clearing agency or for which it is responsible.[80]

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(d)(10). In addition, the Commission requests comments on the following specific issues:

• Is the Commission's proposed rule regarding immobilization and dematerialization of securities certificates and transferring them by book entry to the greatest extent possible sufficiently clear? If not, why not and what would be a better alternative?

• How do current practices of clearing agencies regarding immobilization and dematerialization of securities certificates compare to the practices that the Commission proposes to require in this rule? What are the expected incremental costs to clearing agencies in connection with adding to or revising their current practices in order to implement the Commission's proposed rule?

• What advantages or disadvantages might certificates have over securities

[74] Because clearing agencies are SROs, their rules are published by the Commission and are generally available on each clearing agency's Web site. Nevertheless, discrete rule proposals may not necessarily provide a complete picture of a clearing agency's operations and risk mitigation procedures.

[75] *See* 15 U.S.C. 78q–1(b)(3)(F).

[76] Immobilization refers to any circumstance where an investor does not receive a physical certificate upon the purchase of shares or is required to physically deliver a certificate upon the sale of shares.

[77] Dematerialization is the process of eliminating physical certificates as a record of security ownership.

[78] *See* proposed Rule 17Ad–22(a)(2) for definition of "central securities depository services." In the U.S., DTC is currently the only registered clearing agency that provides central securities depository services.

[79] By concentrating the location of physical securities in a single central securities depository, clearing agencies are able to centralize the operations associated with custody and transfer and reduce costs through economies of scale. Virtually all mutual fund securities, government securities, options, and municipal bonds in the U.S. are dematerialized and most of the equity and corporate bonds in the U.S. market are either immobilized or dematerialized. While the U.S. markets have made great strides in achieving immobilization and dematerialization for institutional and broker-to-broker transactions, many industry representatives believe that the small percentage of securities held in certificated form impose unnecessary risk and expense to the industry and to investors. *See* Exchange Act Release No. 8398 (March 11, 2004), 69 FR 12921 (March 18, 2004).

[80] 15 U.S.C. 78q–1(b)(3)(F).

held in book-entry-only form (*e.g.,* proof of ownership in the event of a loss of electronic records of ownership)? Under what circumstances, if any, should the Commission encourage or discourage the use of physical certifications?

Proposed Rule 17Ad–22(d)(11): Default Procedures

Proposed Rule 17Ad–22(d)(11) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to make key aspects of their default procedures publicly available. The Commission preliminarily believes that this would provide certainty and predictability to market participants about the measures a clearing agency will take in the event of a participant default. Key aspects of a clearing agency's default procedures should generally include the following: (i) The circumstances in which action may be taken (*e.g.,* what events trigger mutualization of losses); (ii) who may take those actions (*e.g.,* division of responsibilities when clearing agencies operate links to other clearing agencies); (iii) the scope of the actions that may be taken (*e.g.,* any limits on the total losses that would be mutualized); (iv) the mechanisms to address a clearing agency's obligations to non-defaulting participants (*e.g.,* process for clearing trades guaranteed by the clearing agency to which a defaulting participant is a party); and (v) the mechanisms to address the defaulting participant's obligations to its customers (*e.g.,* process for dealing with defaulting participants' customer accounts). The proposed rule also would require that clearing agencies establish default procedures that ensure that the clearing agency can take timely action to contain losses and liquidity pressures [81] and to continue meeting its obligations when due in the event of a participant default. Default procedures, among other things, are meant to reduce the likelihood that a default by a participant, or multiple participants, will disrupt the clearing agency's operations. By creating a framework of default procedures that are designed to permit a clearing agency to take actions to contain losses and liquidity pressures it faces while continuing to meet its obligations, the clearing agency should be in a better position to continue providing its services in a manner that promotes accurate clearance and settlement during times of market stress.

The Commission preliminarily believes that the requirements in proposed Rule 17Ad–22(d)(11) would increase the possibility that defaults by participants, should they occur, would proceed in an orderly and transparent manner. This is because the Commission preliminarily believes that the proposed rule would help to ensure that all participants are aware of the default process and are able to plan accordingly and that clearing agencies would have sufficient time to take corrective actions to mitigate potential losses.

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(d)(11). In addition, the Commission requests comments on the following specific issues:

- Is the Commission's proposed rule requiring a clearing agency to establish default procedures and make key aspects of those default procedures publicly available sufficiently clear? If not, why not and what would be a better alternative?
- How do current practices of clearing agencies with respect to default procedures compare to the requirements of the proposed rule? What are the expected incremental costs to clearing agencies in connection with adding to or revising their current practices in order to implement the Commission's proposed rule?
- Should the Commission require specific default procedures for all clearing agencies, or should clearing agencies have discretion to create their own default procedures consistent with the proposed rule? Should the default procedures include a resolution plan if the clearing agency is unable to obtain sufficient financial resources?
- How much flexibility should a clearing agency have in the time it takes to manage a default and perform any liquidation of positions?

Proposed Rule 17Ad–22(d)(12): Timing of Settlement Finality

Proposed Rule 17Ad–22(d)(12) would require clearing agencies establish, implement, maintain and enforce written policies and procedures reasonably designed to ensure that final settlement occurs no later than the end of the settlement day and that intraday or real-time finality is provided where necessary to reduce risks. A clearing agency would be able to comply with this requirement by having a reasonable process for facilitating final settlement to occur no later than the end of the settlement day and for providing intraday or real-time finality where necessary to reduce risks. Intraday or real-time finality may be necessary to reduce risk in circumstances where the lack of intraday or real-time finality may impede the clearing agency's ability to facilitate prompt and accurate clearance and settlement, cause the clearing agency's participants to fail to meet their obligations, or cause significant disruptions in the securities markets.

The Commission preliminarily believes that requiring intraday or real-time finality for settlements, where such requirement is necessary to reduce risks, would facilitate prompt and accurate clearance and settlement by providing certainty that a settlement is final and irrevocable within a timeframe that is commensurate with the level of risk created by the lack of settlement finality. The risks associated with lack of settlement finality stem from the undermining of confidence that transaction obligations will be discharged by the clearing agency or its participants. Moreover, the Commission preliminarily believes that settlement finality should occur not later than the end of the settlement day to limit the volume of outstanding obligations that are subject to settlement at any one time and thereby reduce the settlement risk exposure of participants and the clearing agency.

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(d)(12). In addition, the Commission requests comments on the following specific issues:

- Is the Commission's proposed rule regarding the timing of settlement finality sufficiently clear? If not, why not and what would be a better alternative?
- How do current practices of clearing agencies with respect to settlement finality compare to the practices that the Commission proposes to require in this rule? What are the expected incremental costs to clearing agencies in connection with adding to or revising their current practices in order to implement the Commission's proposed rule?
- What changes, if any, would be created by the requirement under the proposed rule that final settlement occur no later than the end of the settlement day? Does the proposed rule affect certain identifiable categories of market participants differently than others, such as smaller entities or entities with limited operations in the U.S.? If so, how?

[81] A clearing agency may be able to contain liquidity pressures it faces by taking actions to secure additional sources of liquidity or limiting transactions that potentially serve to drain liquidity resources.

• Are there operational, legal or regulatory impediments to intraday or real-time settlement? Will the proposed standard make it harder for clearing agencies to conduct certain types of business for which intraday or real-time finality may be difficult? Are any additional rules or regulations needed to encourage intraday or real-time finality to reduce risks?

• Are there circumstances when the requirements of intraday, real-time or end of day settlement finality proposed by the rule are not feasible or are not beneficial? If so, in what circumstances?

Proposed Rule 17Ad–22(d)(13): Delivery Versus Payment

Proposed Rule 17Ad–22(d)(13) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to eliminate principal risk by linking securities transfers to funds transfers to achieve delivery versus payment ("DVP"). DVP is achieved in the settlement process when the mechanisms facilitating settlement ensure that delivery occurs if and only if payment occurs.[82]

Among other things, DVP eliminates the risk that a party would lose some or its entire principal because payment is made only if securities are delivered. The Commission preliminarily believes that clearing agencies should be required to use this payment method in order to reduce the potential that delivery of the security is not appropriately matched with payment for a security, thereby impeding the clearing agency's ability to facilitate prompt and accurate clearance and settlement. Therefore, the Commission is proposing that clearing agencies be required to link securities transfers to funds transfers in a way that achieves DVP.

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(d)(13). In addition, the Commission requests comments on the following specific issues:

• Is the Commission's proposed rule regarding using DVP to eliminate principal risk by linking securities transfers to funds transfers sufficiently clear? If not, why not and what would be a better alternative?

• How do current practices of clearing agencies for linking securities transfers to funds transfers compare to the practices that the Commission proposes to require in this rule? What are the expected incremental costs to clearing agencies in connection with adding to or revising their current practices in order to implement the Commission's proposed rule?

• What are the advantages and disadvantages of the proposed rule mandating a strict DVP standard? Does the proposed rule affect certain identifiable categories of clearing agencies differently than others, such as clearing agencies with more diversified post-trade services as compared to clearing agencies that specialize in fewer activities?

• Are there operational or legal impediments to implementing the proposed DVP rule? Would the proposed rule make it more difficult for clearing agencies to conduct certain types of business that may require a longer settlement cycle, for reasons outside of the clearing agency's control? Are any additional rules or regulations needed to support achievement of the proposed DVP rule?

• Are there circumstances when DVP is not feasible or practicable? If so, when?

Proposed Rule 17Ad–22(d)(14): Risk Controls To Address Participants' Failure To Settle

Proposed Rule 17Ad–22(d)(14) requires clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to institute risk controls, including collateral requirements and limits to cover the clearing agency's credit exposure to each participant exposure fully, that ensure timely settlement in the event that the participant with the largest payment obligation is unable to settle when the clearing agency provides central securities depository services[83] and extends intraday credit to participants.

Clearing agencies that provide central securities depository services may sometimes extend intraday credit to participants to, among other things, facilitate timely settlements by providing participants with an additional tool to meet delivery obligations. If a participant fails to settle its obligations to the clearing agency, the clearing agency must cover those obligations to be able to continue to facilitate prompt and accurate clearance and settlement.

The Commission preliminarily believes it is important for clearing agencies that provide central securities depository services to institute risk controls, including collateral requirements and limits to cover the clearing agency's credit exposure to each participant exposure fully, that ensure timely settlement in these circumstances to address the risk that the participant may fail to settle after credit has been extended. The Commission also preliminarily believes that requiring the controls to be designed to withstand the inability of the participant with the largest payment obligation to settle, in such circumstances, would reduce the likelihood of disruptions at the clearing agency by having controls in place to account for the largest possible loss from any individual participant and thereby help the clearing agency to provide prompt and accurate clearance and settlement during times of market stress.[84]

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(d)(14). In addition, the Commission requests comments on the following specific issues:

• Is the Commission's proposed rule regarding risk controls to ensure timely settlement for a clearing agency providing central securities depository services sufficiently clear? If not, why not and what would be a better alternative?

• How do current practices of clearing agencies that provide central securities depository services compare to the practices that the Commission proposes to require in this rule? What are the expected incremental costs to clearing agencies in connection with adding to or revising their current practices in order to implement the Commission's proposed rule?

• In addition to collateral requirements and limits on credit exposure to participants, are there other controls on intra-day credit that could be effective in managing settlement risk? If so, should the Commission require the use of any of these other risk controls?

• What are the advantages and disadvantages of requiring that controls be designed to withstand a failure to

[82] *See* Bank for International Settlements, *Delivery Versus Payment in Securities Settlement Systems* (1992), *available at http://www.bis.org/publ/cpss06.pdf.* Three different DVP models can be differentiated according to whether the securities and/or funds transfers are settled on a gross (trade-by-trade) basis or on a net basis.

[83] *See* proposed Rule 17Ad–22(a)(2) for definition of "central securities depository services."

[84] As previously indicated, IOSCO and the CPSS are currently in the process of revising their existing sets of international standards which include those related to a clearing agency's ability to withstand participant failures and to meet payment obligations.

settle by the participant with the largest payment obligation?

• Should the Commission require that the clearing agency be able to withstand a settlement failure by more than the largest participant? For example, should the Commission require the clearing agency be able to withstand a settlement failure by the participants with the two largest payment obligations? Why or why not?

Proposed Rule 17Ad–22(d)(15): Physical Delivery Risks

Proposed Rule 17Ad–22(d)(15) would require clearing agencies establish, implement, maintain and enforce written policies and procedures reasonably designed to disclose to their participants the clearing agency's obligations with respect to physical deliveries.[85] For example, if a clearing agency (as part of its operations) takes physical delivery of securities from its participants in return for payments of cash, then it must inform its participants of the extent of the clearing agency's obligations to make payment. A statement by the clearing agency to its participants about the clearing agency's obligations with respect to physical deliveries, among other things, would help to ensure that participants have information that is likely to enhance the participants' understanding of their rights and responsibilities with respect to using the clearance and settlement services of the clearing agency. The Commission preliminarily believes that providing such information to participants would promote a shared understanding regarding physical delivery practices between the clearing agency and its participants which could help reduce the potential for fails and thereby facilitate prompt and accurate clearance and settlement.

The proposed rule would also require clearing agencies to reasonably design their operations to identify and manage the risks that arise in connection with their obligations for physical deliveries. The risks associated with physical deliveries could stem from, among other factors, operational limitations with respect to assuring receipt of physical deliveries and processing of physical deliveries. The Commission preliminarily believes that requiring clearing agencies to identify and manage these risks would reduce the potential that issues will arise as a result of physical deliveries because the clearing agency will have acted preemptively to deal with potential issues that may disrupt the clearance and settlement process. Accordingly, the Commission preliminarily believes this requirement would help a clearing agency to facilitate prompt and accurate clearance and settlement consistent with Section 17A of the Exchange Act.[86]

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–22(d)(15). In addition, the Commission requests comments on the following specific issues:

• Is the Commission's proposed rule regarding providing information regarding physical delivery and identifying and managing risks associated with physical delivery sufficiently clear? If not, why not and what would be a better alternative?

• How do current practices of clearing agencies with respect to physical delivery compare to the practices that the Commission proposes to require in this rule? What are the expected incremental costs to clearing agencies in connection with adding to or revising their current practices in order to implement the Commission's proposed rule?

• What type of information would be useful for participants to receive from a clearing agency regarding the clearing agency's obligations to participants with respect to physical deliveries? What are the advantages or disadvantages of including specific disclosure requirements with respect to any of this information?

• Are there physical delivery obligations that clearing agencies should not assume or for which the Commission should consider additional restrictions?

*B. Proposed Rule 17Aj–1 Dissemination of Pricing and Valuation Information by Security-Based Swap Clearing Agencies That Perform Central Counterparty Services*

The Commission is proposing Rule 17Aj–1 to incorporate requirements regarding dissemination of pricing and valuation information in the CDS Clearing Exemption Orders into the Commission's rules for security-based swap clearing agencies.[87] Recently, the Commission voted to extend these temporary conditional exemptions from certain provisions of the Federal securities laws until July 16, 2011 to continue to facilitate central clearing of certain CDS.[88] The proposed rule is designed in part to continue the existing dissemination requirements from the CDS Clearing Exemption Orders which would otherwise expire along with those exemption orders.

Proposed Rule 17Aj–1 would require dissemination of pricing and valuation information by security-based swap clearing agencies that perform CCP services.[89] In particular, proposed Rule 17Aj–1 would require each security-based swap clearing agency that performs CCP services to make available to the public, on terms that are fair, reasonable, and not unreasonably discriminatory,[90] all end-of-day settlement prices and any other prices for security-based swaps that the clearing agency may establish to calculate its participants' mark-to-market[91] margin requirements and any

[85] The proposed rule would provide clearing agencies with the flexibility to determine the method by which the clearing agency will state this information to its participants. However, the clearing agencies should take care to develop an approach that provides sufficient notice to its participants regarding the clearing agency's obligations.

[86] 15 U.S.C. 78q–1(b)(3)(F).

[87] *See, e.g.,* the CDS Clearing Exemption Order relating to ICE Trust. "[T]his temporary extension is conditioned on ICE Trust, directly or indirectly, making available to the public on terms that are fair and reasonable and not unreasonably discriminatory: (i) All end-of-day settlement prices and any other prices with respect to Cleared CDS that ICE Trust may establish to calculate mark-to-market margin requirements for ICE Trust clearing members; and (ii) any other pricing or valuation information with respect to Cleared CDS as is published or distributed by ICE Trust." Exchange Act Release No. 63387 (November 29, 2010) 75 FR 75502 (December 3, 2010).

[88] The extensions of the temporary conditional exemptions applied to central clearing of certain CDS by ICE Trust, ICE Clear Europe, CME and Eurex. *See* Exchange Act Release Nos. 63389 (November 29, 2010), 75 FR 75520 (December 3, 2010); 63390 (November 29, 2010), 75 FR 75518 (December 3, 2010); 63388 (November 29, 2010), 75 FR 75522 (December 3, 2010); 63387 (November 29, 2010) 75 FR 75502 (December 3, 2010) (extending the CDS Clearing Exemption Orders for ICE Clear, Eurex, CME and ICE Trust respectively).

[89] Under the proposed rule, security-based swap clearing agencies would be permitted to use different approaches to make certain pricing and valuation information available to the public. For example, some may choose to engage the services of a third-party vendor while others may make the information directly available through the clearing agency's Web site or some other means.

[90] Proposed Rule 17Aj–1 does not prohibit charges that may be assessed with respect to security-based swap clearing agencies making this information available to the public as long as such charges are fair, reasonable, and not unreasonably discriminatory. The fair, reasonable, and not unreasonably discriminatory requirements for open access to information pursuant to proposed Rule 17Aj–1 are consistent with requirements the Commission adopted pursuant to the CDS Clearing Exemption Orders as well as in Rule 603(a) of Regulation NMS which requires all exchanges, alternative trading systems, and other broker-dealers that offer individual data feeds to make the data available on terms that are fair and reasonable and not unreasonably discriminatory. *See* 17 CFR 242.603(a).

[91] In this specific context of the margin practices of security-based swap clearing agencies, the term "mark-to-market" refers to the variation margin practices used by a clearing agency to account for ongoing fluctuations in the market value of its participants' security-based swap positions.

other price or valuation information with respect to security-based swaps as is published or distributed by the clearing agency to its participants.[92] The Commission preliminarily believes this requirement should apply to security-based swap clearing agencies that perform CCP services because, based on the Commission's oversight experience pursuant to the CDS Clearing Exemption Orders, price and valuation information with respect to security-based swaps may often be limited and such a requirement could help to provide information to market participants that may otherwise only be available to the participants of a particular clearing agency. Clearing agencies that clear standard securities may not face similar limitations on price and valuation information. As a result, the Commission is proposing this rule only with respect to security-based swap clearing agencies that perform CCP services but is requesting comment on whether the rule should apply more broadly.

As noted above, the Commission granted the CDS Clearing Exemption Orders to promote the use of CCPs with respect to CDS.[93] Section 763(b) of the Dodd-Frank Act provides that certain security-based swap clearing agencies will be deemed registered for the purpose of clearing security-based swaps ("Deemed Registered Provision").[94] The Deemed Registered Provision becomes effective on July 16, 2011.[95] After the Deemed Registered Provision becomes effective, certain clearing agencies would no longer need an exemption from registration as a clearing agency under Section 17A of the Exchange Act in order to clear security-based swaps.[96] Proposed Rule 17Aj–1 would require securities-based swap clearing agencies that perform CCP services, once registered, to make publicly available the same pricing and valuation information required by the CDS Clearing Exemption Orders.

The clearing agencies operating pursuant to the CDS Clearing Exemption Orders have been generating model end-of-day settlement prices for CDS, which they in turn provide to clearing members and use to establish margin requirements for member positions. Pursuant to the terms of the CDS Clearing Exemption Orders, these clearing agencies have also made this information available to the public. The Commission preliminarily believes that public availability of this information and other related pricing data has helped to improve fairness, efficiency, and market competition by making available to all market participants data that may otherwise be available to only a limited subset of market participants. For example, end-of-day settlement prices generated by security-based swap clearing agencies represent pricing during the lifecycle of a security-based swap. As a result, this end-of-day pricing information would generally not be captured as part of any pre- or post-trade market data and may therefore provide additional information for market participants to consider in determining the value of the same or similar security-based swap positions. Accordingly, the Commission is proposing Rule 17Aj–1 to incorporate the current requirements for dissemination of price and valuation information under the CDS Clearing Exemption Orders.

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Aj–1. In addition, the Commission requests comments on the following specific issues:

- Is the current requirement in the CDS Clearing Exemption Orders to provide certain pricing information helpful in promoting price transparency and efficiency in the CDS market? If so, why? If not, why not? Are there ways in which the requirement could be improved, for instance to ensure better access to those who may want to access the information but find it difficult to obtain?
- Have market participants found the standard to make information available to the public on terms that are fair, reasonable, and not unreasonably discriminatory sufficiently clear? If not, what type of additional guidance would be useful? Should it be expanded to apply to all clearing agencies? Why or why not?
- Is there any other pricing information, such as with respect to valuation of security-based swaps by clearing agencies, that the Commission should consider requiring security-based swap clearing agencies to make available to the public?

*C. Proposed Rule 17Ad–23 Clearing Agency Policies and Procedures To Protect the Confidentiality of Trading Information of Clearing Agency Participants*

The Commission is proposing Rule 17Ad–23 to require all clearing agencies to establish, implement, maintain, and enforce written policies and procedures that are reasonably designed to protect the confidentiality of transaction information received by the clearing agency. Such transaction information may include, but is not limited to, trade data, position data, and any non-public personal information about a clearing agency participant or any of its participants' customers. The Commission preliminarily believes that such policies and procedures would help to limit the potential misuse of confidential information that could impede prompt and accurate clearance and settlement and reduce confidence in the operations of the clearing agency.

The proposed rule also provides that the required written policies and procedures shall include, but are not limited to, (a) limiting access to confidential trading information of clearing members to those employees of the clearing agency who are operating the system or responsible for its compliance with applicable laws or rules and (b) limitations on personal trading by employees and agents of the clearing agency. This proposed requirement would incorporate certain conditions under the CDS Clearing Exemption Orders previously granted to security-based swap clearing agencies related to the confidential treatment of proprietary information of participants.[97] As an intermediary in

[92] Clearing agencies may destroy or otherwise dispose of records at the end of five years consistent with Rule 17a–6 of the Exchange Act. *See* 17 CFR 240.17a–6.

[93] *See* discussion *supra* in Section I.

[94] *See* Public Law 111–203 § 763(b) (adding new Section 17A(l) to the Exchange Act. Under this Deemed Registered Provision, eligible clearing agencies will be required to comply with all requirements of the Exchange Act, and the rules thereunder, applicable to registered clearing agencies to the extent it clears security-based swaps after the effective date of the Deemed Registered Provision, including, for example, the obligation to file proposed rule changes under Section 19(b) of the Exchange Act.

[95] *See* Public Law 111–203 § 774.

[96] ICE Trust, ICE Clear Europe and CME are each eligible for the Deemed Registered Provision based on the specified criteria in Section 763(b) of the Dodd-Frank Act. *See* Exchange Act Release Nos. 63389 (November 29, 2010), 75 FR 75520 (December 3, 2010); 63390 (November 29, 2010), 75 FR 75518 (December 3, 2010); 63388 (November 29, 2010), 75 FR 75522 (December 3, 2010); 63387 (November 29, 2010), 75 FR 75502 (December 3, 2010) (extending the CDS Clearing Exemption Orders for ICE Clear, Eurex, CME and ICE Trust respectively).

[97] *See, e.g.,* CDS Clearing Exemption Order for ICE Trust. "ICE Trust shall establish and maintain adequate safeguards and procedures to protect clearing members' confidential trading information. Such safeguards and procedures shall include: (A) Limiting access to the confidential trading information of clearing members to those employees of ICE Trust who are operating the system or responsible for its compliance with this exemption or any other applicable rules; and (B) establishing and maintaining standards controlling employees of ICE Trust trading for their own accounts. ICE Trust must establish and

Continued

security transactions, a clearing agency receives confidential information which, if not protected, could disclose the terms of market participant's trades, trading strategies, or non-public personal information. The Commission believes that the requirement that clearing agencies operating under the CDS Clearing Exemption Orders develop policies and procedures to limit access to confidential information and develop standards restricting trading that may be based on confidential information has contributed to the formation of more robust controls limiting the potential misuse of confidential information (such as trading based on non-public information) and therefore preliminarily believes that it would be appropriate for all clearing agencies to be subject to these requirements.

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–23. In addition, the Commission requests comments on the following specific issues:

- How do clearing agencies currently maintain confidentiality of the transaction information they receive? How do those practices compare to what the proposed rule requires? What are the expected incremental costs to clearing agencies in connection with adding to or revising their current practices to implement the Commission's proposed rule?
- Is the current requirement in the CDS Clearing Exemption Orders helpful in restricting the misuse of confidential information in the CDS market? If so, why? If not, why not? Are there ways in which the requirement could be improved, for instance by permitting fewer restrictions on access to information within a clearing agency?
- In addition to the types of transaction information discussed, what other kinds of transaction information do clearing agencies receive? To what extent would this information be non-public?
- How do clearing agencies monitor or restrict their employees' and agents' trading activities? What are the advantages or disadvantages of such methods?
- Should the Commission propose any specific restrictions (such as prohibitions on trading) instead of having clearing agencies develop their own policies and procedures?
- Should the Commission require the written policies and procedures of the clearing agency to provide for a clear audit trail of transaction information that is processed by the clearing agency? Please explain.
- Instead of applying this proposed rule to all clearing agencies, should the Commission consider requiring that only certain types of clearing agencies be subject to this requirement (*e.g.,* security-based swap clearing agencies)? Why or why not?

*D. Proposed Rule 17Ad–24: Exemption From Clearing Agency Definition for Certain Registered Securities-Based Swap Dealers and Registered Security-Based Swap Execution Facilities*

Section 3(a)(23)(B) of the Exchange Act currently excludes from the definition of clearing agency certain national securities exchanges, dealers, and certain other entities.[98] These exclusions are designed to limit the potential for overlapping or duplicative requirements that may otherwise be imposed on these regulated entities. Because the Dodd-Frank Act creates new categories of entities in the security-based swap markets that may perform functions similar to the functions performed by the excluded entities under Section 3(a)(23)(B) of the Exchange Act in the traditional securities markets, the Commission is considering whether a similar exclusion from the definition of clearing agency may be warranted.

The Commission preliminarily believes that exemptions from the clearing agency definition with respect to registered security-based swap dealers' and registered security-based swap execution facilities' activities, which are comparable to functions carved out from the definition of clearing agency for dealers and exchanges in the traditional securities markets, is necessary and appropriate, in the public interest, and is consistent with the protection of investors because it would mitigate the potential for overlapping or duplicative requirements consistent with prior exclusions from the definition of the term clearing agency. Accordingly, pursuant to the Commission's authority under Section 36 of the Exchange Act,[99] the Commission is proposing Rule 17Ad–24 to exempt certain registered security-based swap dealers and registered security-based swap execution facilities from the definition of clearing agency.

Specifically, proposed Rule 17Ad–24 would provide that a registered security-based swap dealer would not be considered a clearing agency solely by reason of functions it performs as part of customary dealing activities, or solely because it acts on behalf of a clearing agency or a participant in connection with services performed by the clearing agency. For example, a security-based swap dealer that acts as an intermediary in making payments or deliveries or both in connection with transactions in securities as part of its customary dealing activities would not be considered a clearing agency. The exemptions in proposed Rule 17Ad–24 for security-based swap dealers mirror exclusions already applicable to dealers under Section 3(a)(23)(B) of the Exchange Act.

In addition, proposed Rule 17Ad–24 provides that a registered security-based swap execution facility would not be considered a clearing agency solely because it provides facilities for comparison of data relating to the terms

maintain adequate oversight procedures to ensure that the safeguards and procedures established pursuant to this condition are followed." Exchange Act Release Nos. 59527 (March 6, 2009), 74 FR 10791 (March 12, 2009), Exchange Act Release No. 61119 (December 4, 2009), 74 FR 65554 (December 10, 2009) and Exchange Act Release No. 61662 (March 5, 2010), 75 FR 11589 (March 11, 2010) and 63387 (November 29, 2010), 75 FR 75502 (December 3, 2010).

[98] 15 U.S.C. 78c(a)(23)(B). The term "clearing agency" does not include (i) any Federal Reserve bank, Federal home loan bank, or Federal land bank; (ii) any national securities exchange or registered securities association solely by reason of its providing facilities for comparison of data respecting the terms of settlement of securities transactions effected on such exchange or by means of any electronic system operated or controlled by such association; (iii) any bank, broker, dealer, building and loan, savings and loan, or homestead association, or cooperative bank if such bank, broker, dealer, association, or cooperative bank would be deemed to be a clearing agency solely by reason of functions performed by such institution as part of customary banking, brokerage, dealing, association, or cooperative banking activities, or solely by reason of acting on behalf of a clearing agency or a participant therein in connection with the furnishing by the clearing agency of services to its participants or the use of services of the clearing agency by its participants, unless the Commission, by rule, otherwise provides as necessary or appropriate to assure the prompt and accurate clearance and settlement of securities transactions or to prevent evasion of this title; (iv) any life insurance company, its registered separate accounts, or a subsidiary of such insurance company solely by reason of functions commonly performed by such entities in connection with variable annuity contracts or variable life policies issued by such insurance company or its separate accounts; (v) any registered open-end investment company or unit investment trust solely by reason of functions commonly performed by it in connection with shares in such registered open-end investment company or unit investment trust, or (vi) any person solely by reason of its performing functions described in 15 U.S.C. 78c(a)(25)(E).

[99] 15 U.S.C. 78mm. Section 36 of the Exchange Act authorizes the Commission to conditionally or unconditionally exempt any person, security, or transaction, or any class of classes of persons, securities, or transactions, from any provision or provisions of the Exchange Act or any rule or regulation thereunder, by rule, regulation, or order, to the extent that such exemption is necessary or appropriate in the public interest, and is consistent with the protection of investors.

of settlement of securities transactions effected on such registered security-based swap execution facility. The exemptions in proposed Rule 17Ad–24 for security-based swap execution facilities mirror exclusions applicable to national securities exchanges under Section 3(a)(23)(B) of the Exchange Act.

The Commission cautions, however, that security-based swap dealers and security-based swap execution facilities that engage in clearing agency activities beyond the scope of the proposed exemptions could be considered a clearing agency under the broad definition in Section 3(a)(23) of the Exchange Act. Moreover, other participants in the security-based swap market could also qualify as a clearing agency given the broad definition of clearing agency under the Exchange Act.

If a participant in the security-based swap market qualified as a clearing agency, it would be required to register with the Commission. Section 763(b) of the Dodd-Frank Act adds a new Section 17A(g) to the Exchange Act, which directs entities that use instrumentalities of interstate commerce to perform clearing agency functions for security-based swaps to register with the Commission. The Commission notes that the definition of clearing agency under Section 3(a)(23)(A) of Exchange Act is defined broadly to include any person who:

- Acts as an intermediary in making payments or deliveries or both in connection with transactions in securities;
- Provides facilities for the comparison of data regarding the terms of settlement of securities transactions, to reduce the number of settlements of securities transactions, or for the allocation of securities settlement responsibilities;
- Acts as a custodian of securities in connection with a system for the central handling of securities whereby all securities of a particular class or series of any issuer deposited within the system are treated as fungible and may be transferred, loaned, or pledged by bookkeeping entry, without physical delivery of securities certificates (such as a securities depository); or
- Otherwise permits or facilitates the settlement of securities transactions or the hypothecation or lending of securities without physical delivery of securities certificates (such as a securities depository).[100]

Based on this broad definition, the Commission preliminarily believes that certain service providers that facilitate security-based swap contract management may meet the clearing agency definition. The Commission preliminarily believes the following activities, if engaged in by security-based swap market participants, would qualify these participants as clearing agencies and therefore trigger the statutory requirement to register as clearing agencies: [101]

- *Collateral Management Activities.* Collateral management involves calculating collateral requirements and facilitating the transfer of collateral between counterparties. Entities that calculate net payment obligations among counterparties for security-based swaps and provide instructions for payments, including with respect to quarterly interest, credit events, and upfront fees, are likely acting as an intermediary in making payments or deliveries or both in connection with transactions in securities. As a result of acting as such an intermediary in making payments or deliveries or both in connection with transactions in securities, the Commission preliminarily believes that these entities would fall within the definition of a clearing agency [102] and would generally need to register.
- *Trade Matching Services.* "Matching service" is the term that is used to describe the process whereby an intermediary compares each market participant's trade data regarding the terms of settlement of securities transactions, in order to reduce the number of settlements of securities transactions, or to allocate securities settlement responsibilities. An intermediary that captures trade information regarding a securities transaction and performs an independent comparison of that information which results in the issuance of binding matched terms to the transaction is providing matching services and falls within the definition of clearing agency.[103] As a result of comparing each market participant's trade data regarding the terms of settlement of securities transactions, in order to reduce the number of settlements of securities transactions, or to allocate securities settlement responsibilities, the Commission preliminarily believes that entities providing these trade "matching services" with respect to security-based swaps would meet the statutory definition of a clearing agency [104] and would generally need to register.[105] However, the Commission also preliminarily believes that providing preliminary comparisons, such as those provided by certain affirmation and novation service providers that are followed by independent comparisons that result in the issuance of legally binding matched terms, would generally not fall within the definition of clearing agency. Similarly, the Commission preliminarily believes that reconciliation service providers that function solely to permit parties to reconcile trade information records with their counterparties would generally not fall within the definition of clearing agency.
- *Tear Up/Compression Services ("Tear Up services").*[106] Based on discussions between the Commission staff and market participants, the Commission understands that Tear Up service providers generally operate in the following manner:
  - Tear Up services execute an algorithm seeking to reduce the gross notional value of trades and the total number of trades but do not alter the counterparty risk or market risk associated with the trades beyond specified parameters.
  - When using a Tear Up service, the users send all transactions they are willing to terminate to the service. Each user sets tolerances for counterparty exposures it is willing to absorb and how much money it is willing to pay in trade termination costs. The submitted transactions are matched using an

[100] 15 U.S.C. 78c(a)(23)(A).

[101] The Commission stresses that the functions highlighted herein are not an exhaustive list and urges each security-based swap lifecycle event service provider to consider whether its functions place it within the clearing agency definition.

[102] *See supra* note 98 and accompanying text.

[103] *See also* Exchange Act Release No. 39829 (April 6, 1998), 63 FR 17943 (April 13, 1998) (File No. S7–10–98) ("A vendor that provides a matching service will actively compare trade and allocation information and will issue the affirmed confirmation that will be used in settling the transaction.").

[104] *See supra* note 98 and accompanying text.

[105] *See* Exchange Act Release No. 63727 (January 14, 2011) 76 FR 3859 (January 21, 2011) (discussing generally, at footnotes 20 through 22 and the accompanying text, the confirmation process for security-based swap transactions and the Commission's preliminary expectations about the role of matching services in that setting).

[106] Tear-up or multilateral portfolio trade compression services for OTC derivatives seek to eliminate unnecessary or duplicative trades from the market while maintaining a market participant's overall exposure or risk in the market. This allows dealers to reduce operational risk, freeing up liquidity and capital. By reducing the gross notional outstanding of OTC derivatives in normal times, portfolio trade compression provides effective measures to address the risk associated with uncoordinated, disorderly close-out transactions in individual dealers of the positions of a defaulting major dealer. Compression is offered by several vendors and major market participants are now engaged in regular compression exercises. *See* Financial Stability Board, *Implementing OTC Derivatives Market Reforms,* (October 25, 2010), *available at http://www.Financialstabilityboard.org/publications/r_101025.pdf.*

algorithm and tolerances specified by the user.

○ The service then proposes terminations across all parties who participated, including, payments for termination. The users consider the proposal, check their own records, and, if they choose to accept the proposal, fax or otherwise notify their acceptance to the service. If the service receives acceptances from all users, the transaction is considered binding and the relevant transactions are considered terminated.

○ The users generally exchange payments and confirmations outside the service. The Tear Up service will send the completed files to a third party service provider for matching and the "torn up" transactions are terminated in bulk at the security-based swap data repository. The security-based swap data repository maintains a record of which parties terminated the "torn up" trades.

The Commission preliminarily believes that a Tear Up service provider that performs these functions would generally fall within the definition of clearing agency and would need to register because, among other activities, it would be acting as an intermediary that provides facilities for the comparison of data regarding the terms of settlement of securities transactions, to reduce the number of settlements of securities transactions, or the allocation of securities settlement responsibilities.[107]

The Commission requests comment on all aspects of the proposed exemptions from the definition of clearing agency for registered security-based swap dealers and registered security-based swap execution facilities in proposed Rule 17Ad–24. The Commission also requests comments on which activities fall within the definition of clearing agency, particularly within the context of activities in the security-based swap market. In addition, the Commission requests comments on the following specific issues:

• What are the advantages or disadvantages of the Commission granting the proposed exemptions from the definition of clearing agency? If there are disadvantages to these proposed exemptions, what are they and how do they compare to the benefits?

• Under what circumstances are market participants likely to use the proposed exemptions for registered security-based swap dealers and registered security-based swap execution facilities? Are there any additional terms or conditions that the Commission should consider imposing with respect to the proposed exemptions? Are there any advantages or disadvantages related to the proposed exemptions that the Commission should consider?

• Under Section 17A(b)(3)(I) of the Exchange Act, the rules of a clearing agency should not impose any undue burden on competition. Should the Commission augment this statutory requirement by adopting rules that prohibit clearing agencies from entering into certain types of arrangements? If so, which arrangements, and why? In particular, should the Commission promulgate rules concerning any revenue sharing arrangements used by clearing agencies? Please explain why or why not. Are revenue sharing arrangements common among clearing agencies? How are they used? Are revenue sharing arrangements a manner of directing funds to a subset of clearing members, which funds otherwise could support a general reduction of clearing costs that could be equitably distributed among members? If the Commission adopts rules regarding revenue sharing, what aspects of the revenue sharing arrangements should the rules address and how might the rules be designed to promote competition and fair access to the clearing agency? If the Commission promulgates rules regarding certain arrangements, how should the Commission mitigate the potential risk of unduly limiting the ability of clearing agencies to develop new commercial arrangements?

• Are there any additional entities for which the Commission should consider providing exemptions with respect to the definition of clearing agency, particularly in the context of the security-based swap market? If so, why would providing such exemptions be necessary or appropriate in the public interest, and consistent with the protection of investors? Under what terms and conditions should the Commission consider providing such exemptions?

• Is there additional information about any of the security-based swap services described by the Commission that would affect the consideration of whether these activities trigger the definition of clearing agency?

• Are there any other security-based swap services that may fall within the clearing agency definition? If so, what are those services? Why would they be appropriately classified as clearing agency functions?

• If a security-based swap clearing agency that does not provide CCP services is required to register with the Commission as a clearing agency, are there certain requirements that are applicable or proposed to be applicable to other clearing agencies that should not apply to these security-based swap clearing agencies? For example:

○ Should non-CCP security-based swap clearing agencies be subject to proposed Regulation MC,[108] which the Commission proposed on October 14, 2010 to mitigate the potential conflicts of interest that could exist at certain entities, including security-based swap clearing agencies, through conditions and structures relating to ownership, voting, and governance of these entities? Why or why not? Should proposed Regulation MC apply to some but not all security-based swap clearing agencies that do not provide CCP services? If so, which ones?

○ Should non-CCP security-based swap clearing agencies be subject to proposed Rule 17Ad–25, which would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to identify and address existing or potential conflicts of interest? Why or why not? Should proposed Rule 17Ad–25 apply to some but not all security-based swap clearing agencies that do not provide CCP services? If so, which ones?

○ Should non-CCP security-based swap clearing agencies be subject to proposed Rule 17Ad–26, which would require each clearing agency to establish governance standards for its board or board committee members? Why or why not? Should proposed Rule 17Ad–26 apply to some but not all security-based swap clearing agencies that do not provide CCP services? If so, which ones?

• What are the costs associated with requiring the types of entities described above that do not offer CCP services to register as a clearing agency and operate as an SRO (including compliance with ongoing SRO rule filings requirements)? Please consider both the initial and ongoing costs, and please consider the burdens that such requirements may place on the ability of these entities to operate in a commercially viable manner. Are there competitors who might offer competing services (either in the United States or abroad) without being subject to these requirements? Are these costs offset by regulatory requirements or industry commitments to use certain security-based swap service providers that fall within the definition of a clearing agency? What implications would registration of these entities have for the security-based swap

[107] *See supra* note 98 and accompanying text.

[108] *See* Exchange Act Release No. 63107, 75 FR 65882, *supra* note 45.

markets more generally, and for the availability of their services to market participants?

*E. Proposed Amendment of Rule 17Ab2–1: Registration of Clearing Agencies*

The Commission is proposing to amend Rule 17Ab2–1(c) regarding the registration of clearing agencies. Rule 17Ab2–1(c) currently provides that, if requested by an applicant, the Commission may grant a temporary registration providing for exemptions from certain registration requirements in Section 17A(b)(3) of the Exchange Act. Prior to the Dodd-Frank Act's amendments to the Exchange Act, the Commission was not restricted in its ability to grant exemptions from registration requirements to any category of clearing agencies. Therefore, the exemptions discussed in Rule 17Ab2–1(c) applied with respect to all clearing agencies.

The Dodd-Frank Act amended Section 36 of the Exchange Act and altered the Commission's authority to provide exemptions from the registration requirements applicable to security-based swap clearing agencies pursuant to Section 17A(g) of the Exchange Act.[109] Accordingly, the Commission proposes to amend Rule 17Ab2–1 to reflect these changes. Specifically, the proposal would amend Rule 17Ab2–1(c) to clarify that when granting a temporary registration, the Commission may do so for "a specific period of time and may exempt, other than for purposes of section 17A(g) of the Act, the registrant from one or more of the requirements * * * ". The Commission preliminarily believes this proposed amendment to Rule 17Ab2–1(c), clarifying how the rule would operate in light of changes to the Commission's exemptive authority under Section 36 of the Exchange Act with respect to Section 17A(g) of the Exchange Act, is appropriate given the change to the Commission's exemptive authority under Section 36 of the Exchange Act effected by the Dodd-Frank Act.[110]

The Commission also proposes other technical changes to Rule 17Ab2–1(c) unrelated to the Dodd-Frank Act that the Commission preliminarily believes would help in the administration of the rule pertaining to temporary registrations and would thereby be appropriate in the public interest, for the protection of investors.[111] Specifically, the Commission proposes to amend Rule 17Ab2–1(c) to clarify that the temporary registration may be issued at the discretion of the Commission. The Commission preliminarily believes that the ability to grant a temporary registration provides useful flexibility to further evaluate whether a clearing agency is meeting required standards before granting a permanent registration. Operational, resource, internal control or other issues may only become apparent after a clearing agency has commenced operations. In addition, the proposal would amend the current provision indicating that the Commission may grant the temporary registration for eighteen months or such longer period as the Commission may provide by order, to state that the Commission may grant the temporary registration for twenty-four months or such longer period as the Commission may provide by order.[112] The Commission preliminarily believes that the temporary registration process should explicitly provide greater time to allow the clearing agency to operate before registration becomes final because doing so would enhance the Commission's capacity to provide oversight that promotes prompt and accurate clearance and settlement.

Request for Comment

The Commission generally requests comments on all aspects of the proposed amendments to Rule 17Ab2–1. In addition, the Commission requests comments on the following specific issues:

- Are the proposed changes to Rule 17Ab2–1 setting forth the restrictions on providing exemptions with respect to security-based swap clearing agencies sufficiently clear?
- Would any additional changes to Rule 17Ab2–1 regarding how the clearing agency registration requirements apply with respect to security-based swap clearing agencies be beneficial to market participants?
- What are the advantages and disadvantages of the proposed changes to the temporary registration process, such as stating the temporary registration may be issued at the discretion of the Commission and the revisions to the timeframe for the temporary registration?

*F. Proposed Rule 17Ad–25: Clearing Agency Procedures To Identify and Address Conflicts of Interest*

The Commission is proposing Rule 17Ad–25 to require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to identify and reasonably existing or potential conflicts of interest.[113] For example, there may be actual or potential conflicts of interest between the activities of a clearing agency and the interests of its participants or board members, which could affect decision making by officers or directors or actions by participants in seeking to influence its operations. The proposed rule also would require the clearing agency's policies and procedures to be reasonably designed to minimize conflicts of interest in decision making by the clearing agency.

The Commission preliminarily believes it is important for clearing agencies to evaluate their activities and determine potential sources for conflicts of interests that exist within their organization and to reasonably address such conflicts so that they do not disrupt the clearing agency's ability to facilitate prompt and accurate clearance and settlement. The Commission also preliminarily believes that requiring clearing agencies, under proposed Rule 17Ad–25, to have reasonably designed policies and procedures to minimize conflicts of interest in decision making by the clearing agency would facilitate the development of tailored policies and procedures that mitigate conflicts specific to the clearing agency's business. Moreover, the Commission preliminarily believes the proposed rule would be useful in facilitating its oversight of clearing agencies by providing a documented plan against which the Commission could evaluate a clearing agency's efforts to mitigate conflicts and potentially provide the Commission with a better understanding of the potential sources of conflicts for a specific clearing agency.

[109] *See* Section 772 of Public Law 111–203, 124 Stat. 1376 (2010) amending Section 36 of the Exchange Act.

[110] *Id.*

[111] *See* 15 U.S.C. 78q–1(d).

[112] This change would also include a conforming change to the timing for granting a non-temporary registration.

[113] Proposed Rule 17Ad–25 would complement other applicable requirements concerning conflicts of interests at clearing agencies that may also separately apply. These other requirements include the existing regulatory framework of Section 17A of the Exchange Act and the conflicts-related requirements contemplated by proposed Rule 17Ad–22(d)(8) as well as Section 765 of the Dodd-Frank Act with respect to security-based swap clearing agencies. *See supra* Section III.A. (proposing that clearing agencies be required to have governance arrangements that are clear and transparent to fulfill Exchange Act requirements and to support the objectives of owners and participants and promote the effectiveness of the clearing agency's risk management procedures). *See also* Exchange Act Release No. 63107, 75 FR 65882, *supra* note 45.

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–25. In addition, the Commission requests comments on the following specific issues:

• Under the proposal, clearing agencies would be required to establish, implement, maintain and enforce written policies and procedures reasonably designed to identify and address existing or potential conflicts of interest. Such policies and procedures would also be required to be reasonably designed to minimize conflicts of interest in decision making by the clearing agency. Should the Commission require any specific measures to address conflicts of interests, such as mandating certain boards or board committee compositions with respect to all clearing agencies instead of using a policies and procedures approach? What are the advantages and disadvantages of a more prescriptive approach?

• What, if any, additional guidance by the Commission would be helpful regarding how clearing agencies should evaluate their own activities and determine the potential sources of conflicts?

• Should the Commission consider requiring only certain types of clearing agencies (*e.g.,* security-based swap clearing agencies) to be subject to this requirement? Please explain why or why not. Are there special considerations, such as market concentration, affecting security-based swap clearing agencies that make it particularly important for them to establish, implement, maintain and enforce written policies and procedures to identify and address existing or potential conflicts of interest? If so, what are those special considerations and how would this requirement address them? If not, how would various types of clearing agencies be affected by this requirement? Would there be advantages to maintaining one requirement for all clearing agencies? Why or why not?

*G. Proposed Rule 17Ad–26: Standards for Board or Board Committee Directors*

The Commission is proposing Rule 17Ad–26 to require clearing agencies to establish governance standards for their directors serving on the board or board committees. The Commission preliminarily believes that directors serving on the board and board committees of a clearing agency play a vital role in creating a framework that supports prompt and accurate clearance and settlement because of their role in the decision-making process within a clearing agency. Accordingly, the expertise, diversity of perspectives, conduct and incentives of directors serving on the board and board committees of a clearing agency are likely to affect its effective operation. For example, a lack of expertise by board members or board committee members may deter them from challenging decisions by management and lessen the potential that management will escalate appropriate issues for the board's consideration. In addition, clearing agencies should consider the extent to which persons who have been found to have violated the securities laws, or other similar laws or statutes, may not be fit to serve on the clearing agency's board or board committees. Moreover, a lack of clear guidance as to the roles and responsibilities of directors and procedures for assessing their performance may negatively impact the efficient functioning of the clearing agency.

Therefore, the Commission is proposing Rule 17Ad–26 to require that clearing agencies establish and articulate baseline standards for appointing and retaining their directors, which may help to increase the potential that directors' actions will benefit the clearing organization. The proposed rule specifies that the clearing agency's standards must address the following areas:

• A clear articulation of the roles and responsibilities of directors serving on the clearing agency's board and any board committees;

• Director qualifications providing criteria for expertise in the securities industry, clearance and settlement of securities transactions, and financial risk management; [114]

• Disqualifying factors concerning serious legal misconduct, including violations of the Federal securities laws; and [115]

• Policies and procedures for the periodic review by the board or board committees of the performance of individual members.

The proposed rule would require the clearing agency to clearly articulate the roles and responsibilities of directors serving on the clearing agency's board and any board committees. This would involve the clearing agency setting forth the duties of directors and the functions within the clearing agency for which they are responsible. The Commission preliminarily believes that such a delineation of responsibilities will help to focus directors' efforts to areas that promote the effective operations of a clearing agency.

The proposed rule would also require that the clearing agency establish director qualifications that address the clearing agency's criteria for expertise in the securities industry, clearance and settlement of securities transactions and financial risk management because each of these would have a bearing on the director's ability to understand the operations and risks of a clearing agency. When developing these criteria, clearing agencies could consider the specialized needs of individual board committees, the overall mix of expertise within the board or on a committee, and the benefits of having members with different backgrounds (*e.g.,* regulatory, trading, and risk management experience). The Commission preliminarily believes that this requirement would be beneficial because it could provide greater focus within a clearing agency for the selection of directors that have appropriate expertise, as determined by the clearing agency, which would facilitate the ability of the clearing agency to provide prompt and accurate clearance and settlement.

In addition, the proposed rule would require the development of disqualifying factors concerning serious legal misconduct, including violations of the Federal securities laws. For example, a clearing agency might consider whether to preclude a person

[114] The Commission notes that in other contexts under the Exchange Act certain persons have been required to meet qualification standards. For example, Section 15(b)(7) requires all Commission-registered brokers and dealers to meet such standards of operational capability and all natural persons associated with registered brokers and dealers to meet such standards of training, experience, competence, and such other qualifications as the Commission finds necessary or appropriate in the public interest or for the protection of investors. *See* 15 U.S.C. 78o(b)(7). Section 15(b)(7) permits the Commission to rely on the rules of certain SROs in devising and administering these requirements. For example, the NASD Rule 1000 series contains registration and qualification requirements for registered representatives and principals associated with FINRA-member firms. In addition, NASD Rule 3010 requires all FINRA members to have a supervisory system that provides for, among other things, reasonable efforts to determine that all supervisory personnel are qualified by virtue of experience or training to carry out their assigned responsibilities.

[115] The Exchange Act and the rules promulgated thereunder contain a number of restrictions on the ability of certain registered entities, including clearing agencies, brokers, dealers, transfer agents and other SROs, to be associated with persons subject to a "statutory disqualification," as such term is defined in Section 3(a)(39) of the Exchange Act. 15 U.S.C. 78c(a)(39). For example, Section 17A(b)(4) of the Exchange Act provides that a "registered clearing agency may, and in cases in which the Commission, by order, directs as appropriate in the public interest shall, deny participation to any person subject to a statutory disqualification." 12 U.S.C. 78q–1(b)(4).

who has had a securities license denied, suspended, revoked or restricted by a regulatory authority from serving as a director. The Commission preliminarily believes that such qualification criteria are important with respect to identifying potential issues that would call into question the ability of the persons who are responsible for the governance of the clearing agency to ensure that it complies with applicable laws and regulations.

Finally, the proposed rule would require the clearing agency to establish policies and procedures for the periodic review by the board or a board committee of the performance of its individual members. As previously noted, the Commission preliminarily believes that directors serving on the board or board committees of a clearing agency play a vital role in creating a framework that supports prompt and accurate clearance and settlement because of their role in decision-making processes. Therefore, the Commission preliminarily believes that the board, or a board committee, should establish policies and procedures for the periodic review of the performance of the relevant directors. Such a review should consider the contributions that the directors are making to the clearing agency and to its ability to operate in an effective manner. The policies and procedures for such a review, to be developed by the clearing agency as appropriate given its particular circumstances, might include self-assessments, peer review procedures, or the use of internal or external parties or consultants to facilitate an evaluation of the performance of each relevant director.

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 17Ad–26. In addition, the Commission requests comments on the following specific issues:

- Are there any additional standards for director or board committee members that the Commission should consider requiring? Should any of the requirements in proposed Rule 17Ad–26 be modified or changed? If so, how?
- How direct should the Commission's role be in the oversight and monitoring of the composition and activities of clearing agency boards and board committees? If the Commission's role should be more direct, what mechanisms or structure would facilitate the Commission taking such a role? For example, should the Commission consider any additional requirements related to fiduciary duties to either enhance mitigation of conflicts or address deficiencies?
- What, if any, additional guidance by the Commission would be helpful regarding standards for a clearing agency's directors?
- Should the Commission develop more or less prescriptive requirements regarding standards for directors or board committee members? What are the advantages or disadvantages of any contemplated approach?
- The Commission has previously proposed independence requirements with respect to the board and board committees of security-based swap clearing agencies. Should the boards of all clearing agencies consist of a certain proportion of independent directors? Please explain why or why not.
- Should the Commission require clearing agencies to develop any limits on the type or amount of compensation that directors may receive, such as including prohibiting compensation of independent and other non-management directors from being linked to the business performance of the clearing agency, or being subject to discretion of management? Please explain.
- Should the Commission consider requiring only certain types of clearing agencies (*e.g.,* security-based swap clearing agencies) to be subject to this requirement? Please explain why or why not. Are there special considerations, such as market concentration, affecting security-based swap clearing agencies that make these governance requirements particularly important for them? If so, what are those special considerations and how would this requirement address them? If not, how would clearing agencies that provide different types of clearing services be affected by the application of this requirement? Would there be advantages to maintaining one requirement for all clearing agencies? Why or why not?

*H. Proposed Rule 3Cj–1 Designation of Chief Compliance Officer*

The Dodd-Frank Act amended the Exchange Act to require each clearing agency to appoint a chief compliance officer ("CCO") and specifies the CCO's duties.[116] The Commission is proposing Rule 3Cj–1 to establish requirements concerning a clearing agency's CCO. In particular, proposed Rule 3Cj–1 would incorporate the duties of a clearing agency's CCO that are enumerated in Exchange Act Section 3C(j)[117] and impose additional requirements.

Consistent with the requirements under Section 3C(j) of the Exchange Act, proposed Rule 3Cj–1(a) would require each clearing agency to designate a CCO. The Commission preliminarily believes that a clearing agency would not necessarily need to hire an additional person to serve as its CCO. Instead, a clearing agency could designate an individual already employed by the clearing agency as its CCO.

Consistent with the requirements under Section 3C(j) of the Exchange Act, under proposed Rule 3Cj–1(b), each CCO shall: (1) Report directly to the board or to a senior officer of the clearing agency; (2) in consultation with its board or the senior officer of the registered clearing agency, resolve any conflicts of interest that may arise; (3) be responsible for administering each policy and procedure that is required to be established pursuant to Section 3C of the Exchange Act and rules and regulations thereunder; (4) ensure compliance with the Exchange Act and the rules and regulations thereunder; (5) establish policies and procedures for the prompt remediation of any compliance issues identified by the CCO, and (6) establish and follow appropriate procedures for the prompt handling of management response, remediation, retesting, and closing of non-compliance issues.

In order to clarify the requirements under Section 3C(j) of the Exchange Act, the Commission is also proposing (as part of proposed Rule 3Cj–1(e)) to define the term senior officer for purposes of proposed Rule 3Cj–1 to include the chief executive officer, or other equivalent officer. As the chief executive officer is generally the most senior officer in a clearing agency, the Commission preliminarily believes that such officer should be identified as the responsible individual for purposes of the proposed rule because it would help to promote enhanced focus on compliance issues and thereby potentially lead to more effective operations at a clearing agency.

Consistent with the requirements under Section 3C(j) of the Exchange Act, proposed Rule 3Cj–1(c) would require the CCO to prepare, sign and submit an annual compliance report that describes (i) the compliance of the clearing agency with the Federal securities laws and the rules and regulations thereunder, and (ii) each policy and procedure of the clearing agency (including the code of ethics and conflict of interest policies of

[116] Public Law 111–203, § 763(a) (adding Exchange Act Section 3C(j)).

[117] *Id.*

the registered clearing agency). Also consistent with the requirements under Section 3C(j) of the Exchange Act, proposed Rule 3Cj–1(c) would require the annual compliance report to accompany each appropriate financial report of the clearing agency that is required to be furnished to the Commission pursuant to the Exchange Act and the rules thereunder. Finally, the CCO must certify under penalty of law that the compliance report is accurate and complete.

In addition, to clarify and enhance the requirements under Section 3C(j) of the Exchange Act, the Commission is proposing to require that each annual compliance report:

- Be submitted to the board of directors and audit committee (or equivalent bodies) of the clearing agency promptly after the date of execution of the required certification and prior to filing of the report with the Commission;
- Be filed with the Commission in a tagged data format in accordance with the instructions contained in the EDGAR Filer Manual, as described in Rule 301 of Regulation S–T; [118] and
- Be filed with the Commission within 60 days after the end of the fiscal year covered by such report.

The Commission preliminarily believes it would be appropriate to require that the annual compliance report be submitted to the board of directors and audit committee (or equivalent bodies) prior to filing of the report with the Commission because it would help to focus attention at senior levels of the clearing agency on the contents of the report that is being filed with the Commission. This in turn could help to promote a robust compliance program at the clearing agency by ensuring appropriate attention and response at the Board level.

In addition, the Commission preliminarily believes that it would be appropriate for clearing agencies to file the report with the Commission in a tagged data format in accordance with the instructions contained in the EDGAR Filer Manual in order to provide an electronic system for submitting this report that builds on an existing framework for filings to the Commission. This in turn should help to ease the potential administrative burdens on clearing agencies. As previously noted, the proposed rule would also require that the annual compliance report be filed with the Commission within 60 days after the end of the fiscal year covered by such report. The report would be subject to public availability and the Commission anticipates making such report available through its EDGAR system. The Commission preliminarily believes such time frame would be appropriate because it should give clearing agencies adequate time to review and draft a report based on actions that occurred during the prior year, while also limiting the potential that the information would be stale and thus not be as useful in the Commission's oversight of the clearing agency.

Request for Comment

The Commission generally requests comments on all aspects of proposed Rule 3Cj–1. In addition, the Commission requests comments on the following specific issues:

- Is the definition of "senior officer" appropriate? If not, is it over-inclusive or under-inclusive and how should it be defined?
- Should the Commission include in its proposed rule a requirement that a CCO's compensation must be approved by the board?
- Should the Commission include in its proposed rule a requirement that a CCO may only be removed by action of the board?
- Are there other measures that would further enhance the independence and effectiveness of a CCO and that should be prescribed in a rule, such as requiring that a CCO not perform any other functions?
- Should the Commission impose any additional duties on a CCO of a clearing agency?
- Should the Commission provide guidance in its proposed rules about the CCO's procedures for the remediation of non-compliance issues?
- What is the likely effect of the Commission's proposed rule on the development of the financial markets? Would the proposed rule impede the establishment of clearing agencies?
- Does requiring the compliance report to be filed annually with the Commission within sixty days after the end of the fiscal year covered by such report give a clearing agency enough time to prepare the report? Should the Commission consider a longer or short time frame? Please explain.
- Should the Commission require submission of the CCO compliance report to the board before or after submission to the Commission? How would submission of the compliance report to the board before or after submission to the Commission affect the board's review of the compliance report?
- Should the Commission prescribe any specific method of review by the board with respect to the CCO compliance report? For example, should the Commission require that (i) the CCO compliance report include, as appropriate, recommended actions to be taken by the clearing agency to improve compliance or correct any compliance deficiencies, (ii) the board review any such recommendations and determine whether to approve them, and (iii) the clearing agency notify the Commission if the board declines to approve such recommendations, or approves different actions than those recommended in the CCO compliance report? What are the advantages and disadvantages of such an approach? Should clearing agencies be required to have the CCO report directly to the board instead of also permitting reporting to a senior officer of the clearing agency? What would be the advantages and disadvantages of requiring the CCO to report to the board?

## IV. General Request for Comments

The Commission seeks comment on all aspects of the proposed rules with respect to clearing agencies. The Commission particularly requests comment from the point of view of investors, entities that are registered as clearing agencies, are likely to become registered clearing agencies, entities operating platforms that currently trade or clear security-based swaps, broker-dealers, and financial institutions.

Title VII requires that the SEC consult and coordinate to the extent possible with the CFTC for the purposes of assuring regulatory consistency and comparability, to the extent possible, and states that in adopting rules, the CFTC and SEC shall treat functionally or economically similar products or entities in a similar manner. In the process of developing the proposed rules the Commission staff has consulted with the CFTC staff.

The CFTC is adopting rules related to derivatives clearing organizations ("DCO") in connection with Section 725

[118] The term "tag" (including the term "tagged") refers to an identifier that highlights specific information submitted to the Commission that is in the format required by the EDGAR Filer Manual, as described in Rule 301 of Regulation S–T. *See* 17 CFR 32.301. The term "EDGAR Filer Manual" is defined in Rule 11 of Regulation S–T as "the current version of the manual prepared by the Commission setting out the technical format requirements for an electronic submission." *See* 17 CFR 232.11. If the Commission adopts Rule 3Cj–1 as proposed, it is possible that clearing agencies might be required to file the annual compliance report in paper until such time as an electronic filing system is operational and capable of receiving the annual compliance report. The Commission would notify clearing agencies as soon as the electronic filing system can accept filings of annual compliance reports.

of the Dodd-Frank Act.[119] Understanding that the Commission and the CFTC regulate different products and markets, and as such, appropriately may be proposing alternative regulatory requirements, we request comments on the effect of any differences between the Commission and CFTC approaches to the regulation of clearing agencies and DCOs respectively. Specifically, would the regulatory approaches under the Commission's proposed rulemaking pursuant to Sections 17A(d), 17A(j) and 3C(j) under the Exchange Act and the CFTC's proposed rulemaking pursuant to Section 725 of the Dodd-Frank Act result in duplicative or inconsistent requirements for market participants subject to both regulatory regimes or result in gaps between those regimes? If so, in what ways do commenters believe that such duplication, inconsistencies, or gaps should be minimized? Do commenters believe the approaches proposed by the Commission and the CFTC to govern clearing agencies and DCOs are comparable? If not, why? Do commenters believe there are approaches that would result in more comparable treatment? If so, what are they and what would be the advantages and disadvantages of adopting such approaches? Do commenters believe that it would be appropriate for the Commission to adopt an approach proposed by the CFTC that differs from our proposal? If so, which one?

Commenters should, when possible, provide the Commission with empirical data to support their views. Commenters suggesting alternative approaches should provide comprehensive proposals, including any conditions or limitations that they believe should apply, the reasons for their suggested approaches, and their analysis regarding why their suggested approaches would satisfy the statutory mandates of the Exchange Act with respect to clearing agencies.

## V. Paperwork Reduction Act

Certain provisions of the proposed rules would impose new "collection of information" requirements within the meaning of the Paperwork Reduction Act of 1995 ("PRA").[120] Accordingly, the Commission has submitted the information to the Office of Management and Budget ("OMB") for review in accordance with 44 U.S.C. 3507 and 5 CFR 1320.11. The title of the new collection of information is Clearing Agency Standards for Operation and Governance. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid OMB control number.

### *A. Summary of Collection of Information*

1. Standards for Clearing Agencies

a. Measurement and Management of Credit Exposures

Proposed Rule 17Ad–22(b)(1) contains "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(b)(1) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to measure its credit exposures to its participants at least once each day, and limit its exposures to potential losses from defaults by its participants in normal market conditions so that the operations of the clearing agency would not be disrupted and non-defaulting participants would not be exposed to losses that they cannot anticipate or control.

b. Margin Requirements

Proposed Rule 17Ad–22(b)(2) contains "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(b)(2) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to: (i) Use margin requirements to limit its credit exposures to participants in normal market conditions; (ii) use risk-based models and parameters to set margin requirements; and (iii) review the models and parameters at least monthly.

c. Financial Resources

Proposed Rule 17Ad–22(b)(3) contains "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(b)(3) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to maintain sufficient financial resources to withstand, at a minimum, a default by the participant to which it has the largest exposure in extreme but plausible market conditions, and if the clearing agency provides CCP services for security-based swaps then a default by the two participants to which it has the largest exposures in extreme but plausible market conditions; provided that if a participant controls another participant or is under common control with another participant, then the affiliated participants shall be collectively deemed to be a single participant.

d. Model Validation

Proposed Rule 17Ad–22(b)(4) contains "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(b)(4) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide for an annual model validation consisting of evaluating the performance of the clearing agency's margin models and the related parameters and assumptions associated with such models by a qualified person who does not perform functions associated with the clearing agency's margin models (except as part of the annual model validation) and does not report to such a person.

e. Non-Dealer Access

Proposed Rule 17Ad–22(b)(5) contains "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(b)(5) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide the opportunity for a person that does not perform any dealer or security-based swap dealer services to obtain membership at the clearing agency to clear securities for itself or on behalf of other persons.

f. Portfolio Size and Transaction Volume Thresholds Restrictions

Proposed Rule 17Ad–22(b)(6) contains "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(b)(6) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to have membership standards that do not require that participants maintain a portfolio of any minimum size or that participants maintain a minimum transaction volume.

g. Net Capital Restrictions

Proposed Rule 17Ad–22(b)(7) contains "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(b)(7) would require a clearing agency that provides CCP services to establish,

[119] *See* 75 FR 63113 (October 14, 2010) and 75 FR 77576 (December 13, 2010).

[120] 44 U.S.C. 3501 *et seq.*

implement, maintain and enforce written policies and procedures reasonably designed to provide a person that maintains net capital equal to or greater than $50 million with the ability to obtain membership at the clearing agency, with any net capital requirements being scalable so that they are proportional to the risks posed by the participant's activities to the clearing agency. The proposed rule also permits a clearing agency to provide for a higher net capital requirement (*i.e.,* higher than $50 million) as a condition for membership at the clearing agency if the clearing agency demonstrates to the Commission that such a requirement is necessary to mitigate risks that could not otherwise be effectively managed by other measures, such as scalable limitations on the transactions that the participants may clear through the clearing agency, and the Commission approves the higher net capital requirement as part of a rule filing or clearing agency registration application.

h. Record of Financial Resources

Proposed Rule 17Ad–22(c)(1) contains "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(c)(1) would require that each fiscal quarter (based on calculations made as of the last business day of the clearing agency's fiscal quarter), or at any time upon Commission request, a clearing agency that performs CCP services shall calculate and maintain a record of the financial resources necessary to meet the requirement in proposed Rule 17Ad–22Ad–22(b)(3) and sufficient documentation to explain the methodology it uses to compute such financial resource requirement.

i. Annual Audited Financial Report

Proposed Rule 17Ad–22(c)(2) contains "collection of information requirements" within the meaning of the PRA. Proposed rule 17Ad–22(c)(2) would require a clearing agency to post on its Web site an annual financial report which must (i) be a complete set of financial statements of the clearing agency for the most recent two fiscal years and be prepared in accordance with U.S. GAAP, except that for a clearing agency that is a corporation or other organization incorporated or organized under the laws of any foreign country the financial statements may be prepared according to U.S. GAAP or IFRS, (ii) be audited in accordance with standards of the Public Company Accounting Oversight Board by a registered public accounting firm that is qualified and independent in accordance with rule 2–01 of Regulation S–X (17 CFR 210.2–01), (iii) include a report of the registered public accounting firm that complies with paragraphs (a) through (d) of Rule 2–02 of Regulation S–X (17 CFR 210.2–02).

j. Transparent and Enforceable Rules and Procedures

Proposed Rule 17Ad–22(d)(1) contains "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(d)(1) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide for a well founded, transparent, and enforceable legal framework for each aspect of its activities in all relevant jurisdictions.

k. Participation Requirements

Proposed Rule 17Ad–22(d)(2) contains "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(d)(2) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to require participants to have sufficient financial resources and robust operational capacity to meet obligations arising from participation in the clearing agency. Clearing agencies would also be required to have procedures in place to monitor that participation requirements are met on an ongoing basis, and to have participation requirements that are objective, publicly disclosed, and permit fair and open access.

l. Custody of Assets and Investment Risk

Proposed Rule 17Ad–22(d)(3) contains "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(d)(3) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to hold assets in a manner that minimizes risk of loss or delay in access to them and to invest assets in instruments with minimal credit, market, and liquidity risks.

m. Identification and Mitigation of Operational Risk

Proposed Rule 17Ad–22(d)(4) contains "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(d)(4) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to: (i) Identify sources of operational risk and minimize them through the development of appropriate systems, controls, and procedures; (ii) implement systems that are reliable, resilient and secure, and have adequate, scalable capacity; and (iii) have business continuity plans that allow for timely recovery of operations and fulfillment of a clearing agency's obligations.

n. Money Settlement Risks

Proposed Rule 17Ad–22(d)(5) would contain "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(d)(5) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to employ money settlement arrangements that eliminate or strictly limit the clearing agency's settlement bank risks, that is, its credit and liquidity risks from the use of banks to effect money settlements with its participants, and require funds transfers to the clearing agency to be final when effected.

o. Cost-Effectiveness

Proposed Rule 17Ad–22(d)(6) would contain "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(d)(6) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to be cost-effective in meeting the requirements of participants while maintaining safe and secure operations.

p. Links

Proposed Rule 17Ad–22(d)(7) would contain "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(d)(7) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to evaluate the potential sources of risks that can arise when the clearing agency establishes links either cross-border or domestically to clear trades and ensure that the risks are managed prudently on an ongoing basis.

q. Governance

Proposed Rule 17Ad–22(d)(8) would contain "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(d)(8) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent to fulfill the public interest requirements in Section 17A of the Exchange Act applicable to clearing

agencies, to support the objectives of owners and participants, and to promote the effectiveness of the clearing agency's risk management procedures.

r. Information on Services

Proposed Rule 17Ad–22(d)(9) would contain "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(d)(9) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide market participants with sufficient information for them to identify and evaluate the risks and costs associated with using their services.

s. Immobilization and Dematerialization of Stock Certificates

Proposed Rule 17Ad–22(d)(10) would contain "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(d)(10) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to immobilize or dematerialize securities certificates and transfer them by book entry to the greatest extent possible if the clearing agency performs central securities depository services.

t. Default Procedures

Proposed Rule 17Ad–22(d)(11) would contain "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(d)(11) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to make key aspects of the clearing agency's default procedures publicly available and to establish default procedures that ensure that the clearing agency can take timely action to contain losses and liquidity pressures and to continue meeting its obligations in the event of a participant default.

u. Timing of Settlement Finality

Proposed Rule 17Ad–22(d)(12) would contain "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(d)(12) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to ensure that final settlement occurs no later than the end of the settlement day and that intraday or real-time finality is provided where necessary to reduce risks.

v. Delivery Versus Payment

Proposed Rule 17Ad–22(d)(13) would contain "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(d)(13) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to eliminate principal risk linking securities transfers to funds transfers in a way that achieves DVP.

w. Risk Controls To Address Participants' Failure To Settle

Proposed Rule 17Ad–22(d)(14) would contain "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(d)(14) would require clearing agencies that perform central securities depository services to establish, implement, maintain and enforce written policies and procedures reasonably designed to institute risk controls when the clearing agency extends intraday credit to participants, including collateral requirements and limits to cover the clearing agency's credit exposure to each participant fully, and that ensure timely settlement in the event that the participant with the largest payment obligation is unable to settle. If a participant controls another participant or is under common control with another participant, then the affiliated participants shall be collectively deemed to be a single participant.

x. Physical Delivery Risks

Proposed Rule 17Ad–22(d)(15) would contain "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–22(d)(15) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to state to its participants the clearing agency's obligations with respect to physical deliveries. Clearing agencies would also be required to identify and manage the risks that arise in connection with these obligations.

2. Dissemination of Pricing and Valuation Information by Security-Based Swap Clearing Agencies That Perform Central Counterparty Services

Proposed Rule 17Aj–1 contains "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Aj–1 is designed to preserve the information dissemination requirement from the CDS Clearing Exemption Orders.[121] The proposed rule would require every security-based swap clearing agency that performs CCP services to make available to the public all end-of-day settlement prices and any other prices with respect to security-based swaps that it may use to calculate mark-to-market[122] margin requirements for its participants. Proposed Rule 17Aj–1 also would require every security-based swap clearing agency that performs CCP services to make available to the public any other pricing or valuation information with respect to security-based swaps that it otherwise publishes or makes available to its participants. Proposed Rule 17Aj–1 would not require that this information be made available to the public free of charge. Instead, it would require that the information be provided to the public on terms that are fair, reasonable and not unreasonably discriminatory.

3. Clearing Agency Policies and Procedures To Protect the Confidentiality of Trading Information of Clearing Agency Participants

Proposed Rule 17Ad–23 contains "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–23 would require each registered clearing agency to establish, implement, maintain and enforce written policies and procedures designed to protect the confidentiality of any and all transaction information that the clearing agency receives. Such transaction information may include, but is not limited to, trade data, position data, and any non-public personal information about a clearing agency member or participant or any of its members' or participants' customers. The proposed rule also provides that the required policies and procedures shall include, but are not limited to, (a) limiting access to confidential trading information of clearing members to those employees of the clearing agency who are operating the system or responsible for its compliance with any other applicable laws or rules and (b) standards controlling employees and agents of the clearing agency trading for their personal benefit or the benefit of others.

[121] *See generally* note 6 (providing citations to the CDS Clearing Exemption Orders).

[122] *See supra* note 91 (explaining that in the specific context of the margin practices of security-based swap clearing agencies, the term "mark-to-market" implies the variation margin practices used by the clearing agency to account for ongoing fluctuations in the market value of its participants' security-based swap positions).

4. Exemption From Clearing Agency Definition for Certain Registered Securities-Based Swap Dealers and Registered Security-Based Swap Execution Facilities

Proposed Rule 17Ad–24 provides that a registered security-based swap dealer would not be considered a clearing agency solely by reason of functions performed by such institution as part of customary dealing activities, or solely because it acts on behalf of a clearing agency or a participant in connection with services performed by the clearing agency. In addition, proposed Rule 17Ad–24 provides that a registered security-based swap execution facility would not be considered a clearing agency solely because it provides facilities for comparison of data relating to the terms of settlement of securities transactions. Accordingly, the rule does not impose recordkeeping or information collection requirements, or other collections of information that require approval of the OMB under 44 U.S.C. 3501, *et seq.* Thus, it would not be a "collection of information" within the meaning of the PRA.

5. Registration of Clearing Agencies

The proposed amendment to Rule 17Ab2–1 would mainly clarify that when granting a temporary registration the Commission may do so for "a specific period of time and may exempt, other than for purposes of Section 17A(g) of the Act, the registrant from one or more of the requirements * * *". Accordingly, the proposed rule does not impose recordkeeping or information collection requirements, or other collections of information that require approval of the OMB under 44 U.S.C. 3501, *et seq.* Thus, it would not be a "collection of information" within the meaning of the PRA.

6. Clearing Agency Procedures To Identify and Address Conflicts of Interest

Proposed Rule 17Ad–25 contains "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–25 would require each clearing agency to establish, implement, maintain and enforce written policies and procedures reasonably designed to identify and address existing or potential conflicts of interest, as well as that address methods of minimizing conflicts of interest in decision-making at the clearing agency.

7. Standards for Board or Board Committee Directors

Proposed Rule 17Ad–26 contains "collection of information requirements" within the meaning of the PRA. Proposed Rule 17Ad–26 outlines the proposed standards that would a registered clearing agency would be required to establish for its board members and board committee members. These standards include at least the following areas: (i) A clear articulation of the roles and responsibilities of directors serving on the clearing agency's board and any board committees; (ii) director qualifications providing criteria for expertise in the securities industry, clearance and settlement of securities transactions, and financial risk management; (iii) disqualifying factors concerning serious legal misconduct, including violations of the Federal securities laws; and (iv) policies and procedures for the periodic review by the board or a board committee of the performance of its individual members.

8. Designation of Chief Compliance Officer

Proposed Rule 3Cj–1 contains "collection of information requirements" within the meaning of the PRA. Proposed Rule 3Cj–1 would require each registered clearing agency to designate a CCO. Under proposed Rule 3Cj–1(b), the CCO would be responsible for, among other matters, establishing policies and procedures for the remediation of non-compliance issues identified by the CCO and establishing and following appropriate procedures for the prompt handling of management response, remediation, retesting, and closing of compliance issues.

Under Proposed Rule 3Cj–1(c), the CCO would also be responsible for preparing and signing an annual compliance report that contains a description of (i) the compliance of the clearing agency with respect to the Federal securities laws and the rules and regulations thereunder, and (ii) each policy and procedure of the clearing agency of the compliance officer (including the code of ethics and conflict of interest policies of the registered clearing agency). This compliance report must accompany each appropriate financial report of the clearing agency that is required to be furnished to the Commission pursuant to the Exchange Act and the rules thereunder and include a certification that, under penalty of law, the compliance report is accurate and complete.

Additionally, the compliance report would be required to: (i) Be submitted to the board of directors and audit committee (or equivalent bodies) of the clearing agency promptly after the date of execution of the required certification and prior to filing of the report with the Commission, (ii) be filed with the Commission in a tagged data format in accordance with the instructions contained in the EDGAR Filer Manual as described in Rule 301 of Regulation S–T, and (iii) be filed with the Commission within 60 days after the end of the fiscal year covered by such report.

*B. Proposed Use of Information*

1. Standards for Clearing Agencies

a. Measurement and Management of Credit Exposures

As discussed above, proposed Rule 17Ad–22(b)(1) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to measure its credit exposures to its participants at least once each day, and limit its exposures to potential losses from defaults by its participants in normal market conditions so that the operations of the clearing agency would not be disrupted and non-defaulting participants would not be exposed to losses that they cannot anticipate or control. The purpose of the collection of information is to enable the clearing agency to monitor and limit its exposures to its participants.

b. Margin Requirements

As discussed above, proposed Rule 17Ad–22(b)(2) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to: (i) Use margin requirements to limit its credit exposures to participants in normal market conditions; (ii) use risk-based models and parameters to set margin requirements; and (iii) review the models and parameters at least monthly. The purpose of the collection of information is to enable the clearing agency to maintain sufficient collateral or margin.

c. Financial Resources

As discussed above, proposed Rule 17Ad–22(b)(3) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to maintain sufficient financial resources to withstand, at a minimum, a default by the participant to which it has the largest exposure in extreme but plausible market conditions, and if the clearing agency provides CCP services for security-based swaps then a default by the two participants to which it has the largest exposures in extreme but

plausible market conditions; provided that if a participant controls another participant or is under common control with another participant, the affiliated participant and the participant shall be deemed to be a single participant. The purpose of the collection of information is to enable the clearing agency to satisfy all of its settlement obligations in the event of a participant default.

d. Model Validation

As discussed above, proposed Rule 17Ad–22(b)(4) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide for an annual model validation. The purpose of the collection of information is to enable the clearing agency to obtain an assessment of its margin model by a qualified, independent person.

e. Non-Dealer Access

As discussed above, proposed Rule 17Ad–22(b)(5) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide the opportunity for a person that does not perform any dealer or security-based swap dealer services to obtain membership at the clearing agency to clear securities for itself or on behalf of other persons. The purpose of the collection of information is to enable more market participants to obtain indirect access to clearing agencies.

f. Portfolio Size and Transaction Volume Restrictions

As discussed above, proposed Rule 17Ad–22(b)(6) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to have membership standards that do not require that participants maintain a portfolio of any minimum size or that participants maintain a minimum transaction volume. The purpose of the collection of information is to remove unnecessary barriers to participation in clearing agencies that provide CCP services.

g. Net Capital Restrictions

As discussed above, proposed Rule 17Ad–22(b)(7) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide a person that maintains net capital equal to or greater than $50 million with the ability to obtain membership at the clearing agency, with any net capital requirements being scalable so that they are proportional to the risks posed by the participant's activities to the clearing agency. The rule also permits a clearing agency to provide for a higher net capital requirement (*i.e.,* higher than $50 million) as a condition for membership at the clearing agency if the clearing agency demonstrates to the Commission that such a requirement is necessary to mitigate risks that could not otherwise be effectively managed by other measures, such as scalable limitations on the transactions that the participants may clear through the clearing agency, and the Commission approves the higher net capital requirement as part of a rule filing or clearing agency registration application. The purpose of the collection of information is to remove unnecessary barriers to clearing access by market participants with a net capital level above $50 million, while at the same time facilitating sound risk management practices by clearing agencies by encouraging them to examine and articulate the benefits that higher net capital requirements would create through having clearing agencies develop scalable membership standards that links the activities any participants could potentially engage in with the potential risks posed by the participant.

h. Record of Financial Resources

As discussed above, proposed Rule 17Ad–22(c)(1) would require that each fiscal quarter (based on calculations made as of the last business day of the clearing agency's fiscal quarter), or at any time upon Commission request, a clearing agency that performs CCP services shall calculate and maintain a record of the financial resources necessary to meet the requirement in proposed Rule 17Ad–22c)(3) and sufficient documentation to explain the methodology it uses to compute such financial resource requirement. The purpose of the collection of information is to enable the Commission to monitor the financial resources of clearing agencies that provide CCP services.

i. Annual Audited Financial Report

As discussed above, proposed Rule 17Ad–22(c)(2) would require a clearing agency that provides CCP services to post on its Web site an annual audited financial report that must (i) be a complete set of financial statements of the clearing agency for the most recent two fiscal years and be prepared in accordance with U.S. GAAP, except that for a clearing agency that is a corporation or other organization incorporated or organized under the laws of any foreign country the financial statements may be prepared according to U.S. GAAP or IFRS; (ii) be audited in accordance with standards of the Public Company Accounting Oversight Board by a registered public accounting firm that is qualified and independent in accordance with rule 2–01 of Regulation S–X (17 CFR 210.2–01); and (iii) include a report of the registered public accounting firm that complies with paragraphs (a) through (d) of Rule 2–02 of Regulation S–X (17 CFR 210.2–02). The purpose of the collection of information is to enable the Commission to monitor the financial resources of clearing agencies that provide CCP services.

j. Transparent and Enforceable Rules and Procedures

As discussed above, proposed Rule 17Ad–22(d)(1) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide for a well founded, transparent, and enforceable legal framework for each aspect of their activities in all relevant jurisdictions. The purpose of the collection of information is to help ensure that clearing agencies' policies and procedures do not cause confusion or legal uncertainty among their participants because they are unclear, incomplete or conflict with other applicable laws or judicial precedent.

k. Participation Requirements

As discussed above, proposed Rule 17Ad–22(d)(2) has three principle requirements related to establishing, implementing, maintaining and enforcing written policies and procedures for participation requirements. First, it would require clearing agencies to require participants to have sufficient financial resources and robust operational capacity to meet their obligations. The purpose of the collection of information is to enable clearing agencies to ensure that only persons with sufficient financial and operational capacity are direct participants. Second, clearing agencies would be required to have procedures in place to monitor that participation requirements are met on an ongoing basis. The purpose of the collection of information is to help clearing agencies identify a participant experiencing financial difficulties before the participant fails to meet its settlement obligations. Third, a clearing agency's participation requirements would have to be objective, publicly disclosed, and permit fair and open access. The purpose of the collection of information is to ensure that all qualified persons

can access a clearing agency's services on an equivalent basis.

l. Custody of Assets and Investment Risk

As discussed above, proposed Rule 17Ad–22(d)(3) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to hold assets in a manner that minimizes risk of loss or delay in access to them, and to invest assets in instruments with minimal credit, market, and liquidity risks. The purpose of the collection of information is to enable clearing agencies to access their financial resources quickly so that they settle securities transactions on time and at the agreed upon terms.

m. Identification and Mitigation of Operational Risk

As discussed above, proposed Rule 17Ad–22(d)(4): Would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to: (i) Identify sources of operational risk and minimize them through the development of appropriate systems, controls, and procedures; (ii) implement systems that are reliable, resilient and secure, and have adequate, scalable capacity; and (iii) have business continuity plans that allow for timely recovery of operations and fulfillment of a clearing agency's obligations. The purpose of the collection of information is to ensure that clearing agencies can maintain operations in the event of an operational problem, natural disaster or other similar event.

n. Money Settlement Risks

As discussed above, proposed Rule 17Ad–22(d)(5) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to employ money settlement arrangements that eliminate or strictly limit the clearing agency's settlement bank risks, that is, its credit and liquidity risks from the use of banks to effect money settlements with its participants, and require funds transfers to the clearing agency to be final when effected. The purpose of the collection of information is to promote reliability in a clearing agency's settlement operations.

o. Cost-Effectiveness

As discussed above, proposed Rule 17Ad–22(d)(6) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to be cost-effective in meeting the requirements of participants while maintaining safe and secure operations. The purpose of the collection of information is to help ensure that the services of clearing agencies do not become too expensive.

p. Links

As discussed above, proposed Rule 17Ad–22(d)(7) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to evaluate the potential sources of risks that can arise when the clearing agency establishes links either cross-border or domestically to clear trades, and ensure that the risks are managed prudently on an ongoing basis. The purpose of the collection of information is to help ensure that clearing agencies adequately assess the risks associated with establishing a link with another clearing organization.

q. Governance

As discussed above, proposed Rule 17Ad–22(d)(8) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent to fulfill the public interest requirements in Section 17A of the Exchange Act applicable to clearing agencies; to support the objectives of owners and participants; and to promote the effectiveness of the clearing agency's risk management procedures. The purpose of the collection of information is to promote boards of directors that exercise sufficient oversight of the clearing agency's management and appropriately represent the interests of relevant stakeholders.

r. Information on Services

As discussed above, proposed Rule 17Ad–22(d)(9) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide market participants with sufficient information for them to identify and evaluate the risks and costs associated with using their services. The purpose of the collection of information is to help market participants identify the risks and costs associated with using the clearing agency and would allow market participants to make informed decisions about the use of the clearing agency and take appropriate actions to mitigate their risks and costs associated with the use of the clearing agency.

s. Immobilization and Dematerialization of Stock Certificates

As discussed above, proposed Rule 17Ad–22(d)(10) would require clearing agencies that perform central securities depository services to establish, implement, maintain and enforce written policies and procedures reasonably designed to immobilize or dematerialize securities certificates and transfer them by book entry to the greatest extent possible. The purpose of the collection of information is to enable clearing agencies to promote greater efficiency in the settlement of securities transactions and reduce risk by transferring securities by book entry movements.

t. Default Procedures

As discussed above, proposed Rule 17Ad–22(d)(11) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to make key aspects of their default procedures publicly available and to establish default procedures that ensure that the clearing agency can take timely action to contain losses and liquidity pressures and to continue meeting its obligations in the event of a participant default. The purpose of the collection of information is to foster a greater understanding by market participants of possible steps a clearing agency may take when a participant defaults and possibly reduce the likelihood of market participants taking actions based on incorrect information.

u. Timing of Settlement Finality

As discussed above, proposed Rule 17Ad–22(d)(12) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to ensure that final settlement occurs no later than the end of the settlement day and require that intraday or real-time finality be provided where necessary to reduce risks. The purpose of the proposed rule is to promote consistent standards of timing and reliability in the settlement process.

v. Delivery Versus Payment

As discussed above, proposed Rule 17Ad–22(d)(13) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to eliminate principal risk by linking securities transfers to funds transfers in a way that achieves delivery versus payment. The purpose of the proposed rule is to eliminate principal risk in the transfer of securities and funds.

w. Risk Controls To Address Participant's Failure To Settle

As discussed above, proposed Rule 17Ad–22(d)(14) would require clearing agencies that perform central securities depository services and extend intraday credit to participants to establish, implement, maintain and enforce written policies and procedures reasonably designed to institute risk controls, including collateral requirements and limits to cover the clearing agency's credit exposure to each participant fully, and ensure timely settlement in the event that the participant with the largest payment obligation is unable to settle. The purpose of the collection of information is to enable clearing agencies to satisfy their settlement obligations on time and for the agreed upon terms.

x. Identification and Management of Physical Delivery Risks

As discussed above, proposed Rule 17Ad–22(d)(15) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to state to their participants the clearing agency's obligations with respect to physical deliveries and to identify and manage the risks that arise in connection with these obligations. The purpose of the collection of information is to provide the clearing agency's participants with sufficient information to evaluate the risks and costs associated with participation in the clearing agency.

2. Dissemination of Pricing and Valuation Information by Security-Based Swap Clearing Agencies That Perform Central Counterparty Services

As discussed above, proposed Rule 17Aj–1 would require security-based swap clearing agencies that perform CCP services to make available to the public all end-of-day settlement prices and any other prices with respect to security-based swaps that it may use to calculate mark-to-market margin requirements for its participants and any other pricing or valuation information with respect to security-based swaps that it otherwise publishes or makes available to its participants. The purpose of the collection of information is to help improve fairness, efficiency and market competition by providing market participants and, more generally, the public with a source of pricing data on security-based swaps that may otherwise be difficult to obtain.

3. Clearing Agency Policies and Procedures To Protect the Confidentiality of Trading Information of Clearing Agency Participants

As discussed above, proposed Rule 17Ad–23 would require each registered clearing agency to establish, implement, maintain and enforce written policies and procedures designed to protect the confidentiality of any and all transaction information that the clearing agency receives. Such transaction information may include, but is not limited to, trade data, position data, and any non-public personal information about a clearing agency member or participant or any of its members or participant's customers. The proposed rule also provides that the required policies and procedures shall include, but are not limited to: (a) Limiting access to confidential trading information of clearing members to those employees of the clearing agency who are operating the system or responsible for its compliance with any other applicable laws or rules and (b) standards controlling employees and agents of the clearing agency trading for their personal benefit or the benefit of others. The purpose of the collection of information is to foster confidence in clearing agencies by market participants.

4. Clearing Agency Procedures To Identify and Address Conflicts of Interest

As discussed above, proposed Rule 17Ad–25 would require each registered clearing agency to establish, implement, maintain and enforce written policies and procedures reasonably designed to identify and address existing or potential conflicts of interest and that are reasonably designed to minimize conflicts of interest in decision-making at the clearing agency. The purpose of the collection of information is to enable the Commission to examine and evaluate a clearing agency's efforts to minimize conflicts and help to ensure the transparent, equitable operation of the clearing agency.

5. Standards for Board or Board Committee Directors

As discussed above, proposed Rule 17Ad–26 would require that a registered clearing agency establish certain governance standards applicable to its board or board committee members. The proposed collection of information is to help improve the effectiveness of a clearing agency's board of directors.

6. Designation of Chief Compliance Officer

As discussed above, proposed Rule 3Cj–1 would require each registered clearing agency to designate a CCO who would establish and oversee the implementation of certain policies and procedures relating to non-compliance issues, as well as prepare, sign and submit an annual compliance report. The proposed collection of information should promote better compliance by clearing agencies with all applicable laws, regulations and policies.

*C. Respondents*

1. Standards in Proposed Rule 17Ad–22(b) That Impose a PRA Burden

The standards in proposed Rule 17Ad–22(b) that the Commission preliminarily believes impose a PRA burden are 17Ad–22(b)(1), (2), (3), (4), (5), (6) and (7). The requirements in proposed Rules 17Ad–22(b)(1), (2), (3), (4), (5), (6) and (7) would apply to all clearing agencies that perform central counterparty services. There are currently four clearing agencies authorized to provide CCP services for security-based swap transactions pursuant to the CDS Clearing Exemption Orders.[123] The Commission estimates, based on staff discussions with industry representatives, that there could conceivably be one or two more entities that clear security-based swaps in the future. Thus, the Commission estimates that four to six clearing agencies may seek to clear security-based swaps.[124] The Commission is using the higher estimate of six security-based swap clearing agencies for this PRA analysis. There are also eleven additional clearing agencies currently registered with the Commission,[125] of which only three are currently performing central counterparty services. Thus, for these provisions, the Commission estimates that there would be nine respondents.[126]

[123] *See supra* note 6.

[124] The Commission preliminarily believes that there is a potential for new security-based swap clearing agencies to form but does not expect there to be a large number based on the significant level of capital and other financial resources needed for the formation of a clearing agency.

[125] There are four clearing agencies with active operations currently registered with the Commission, plus seven registered clearing agencies that are inactive. Although the inactive entities may not be acting as clearing agencies, for purposes of the PRA the Commission is estimating 11 total clearing agencies.

[126] This figure was calculated as follows: 6 clearing agencies providing CCP services for security-based swaps + 3 registered clearing agencies providing CCP services = 9 respondent clearing agencies.

2. Standards in Proposed Rule 17Ad–22(c) That Impose a PRA Burden

The standards in proposed Rule 17Ad–22(c) that the Commission preliminarily believes impose a PRA burden are 17Ad–22(c)(1) and (2). The requirements of proposed Rule 17Ad–22(c)(1) would apply to all clearing agencies that perform CCP services. As noted above, there are currently four clearing agencies authorized to provide CCP services for security-based swap transactions pursuant to the CDS Clearing Exemption Orders,[127] and there could conceivably be one or two more entities that clear security-based swaps in the future. Thus, the Commission estimates that four to six clearing agencies may seek to clear security-based swaps.[128] The Commission is using the higher estimate of six respondent clearing agencies for this PRA analysis. There are also eleven additional clearing agencies currently registered with the Commission,[129] of which only three are currently performing central counterparty services. Thus, for proposed Rule 17Ad–22(c)(1), the Commission estimates that there would be nine respondents.[130]

The requirements of proposed Rule 17Ad–22(c)(2) would apply to all clearing agencies. Therefore, the Commission preliminarily believes that these PRA burdens would be imposed on all clearing agencies registered with the Commission. As noted above, there are currently four clearing agencies authorized to clear security-based swaps pursuant to the CDS Clearing Exemption Orders.[131] The Commission estimates, based on staff discussions with industry representatives, that there could conceivably be one or two more entities that clear security-based swaps in the future. Thus, the Commission estimates that four to six clearing agencies may seek to clear security-based swaps.[132] The Commission is using the higher estimate of six for the PRA analysis. There are also eleven additional clearing agencies currently registered with the Commission.[133] Thus, for proposed Rule 17Ad–22(c)(2), the Commission estimates that there would be seventeen respondents.[134]

[127] *See supra* note 6.

[128] *See supra* note 124 and accompanying text.

[129] *See supra* note 125.

[130] *See supra* note 126.

[131] *See supra* note 6.

[132] *See supra* note 124 and accompanying text.

[133] *See supra* note 125.

[134] This figure was calculated as follows: 6 clearing agencies providing CCP services for security-based swaps + 11 additional registered clearing agencies = 17 respondent clearing agencies.

3. Standards in Proposed Rule 17Ad–22(d) That Impose a PRA Burden

In proposed Rule 17Ad–22(d), the requirements that the Commission preliminarily believes impose a PRA burden are 17Ad–22(d)(1), (2), (3), (4), (5), (6), (7), (8), (9), (10), (11), (12), (13), (14) and (15). The Commission preliminarily believes that these PRA burdens would be imposed on all clearing agencies registered with the Commission. As noted above, there are currently four clearing agencies authorized to clear security-based swaps pursuant to the CDS Clearing Exemption Orders.[135] The Commission estimates based on staff discussions with industry representatives, that there could conceivably be one or two more entities that clear security-based swaps in the future. Thus, the Commission estimates that four to six clearing agencies may seek to clear security-based swaps.[136] The Commission is using the higher estimate of six for the PRA analysis. There are also eleven additional clearing agencies currently registered with the Commission.[137] Thus, for these provisions, the Commission estimates that there would be seventeen respondents.[138]

4. Dissemination of Pricing and Valuation Information by Security-Based Swap Clearing Agencies That Perform Central Counterparty Services

The requirements of proposed Rule 17Aj–1 to disseminate pricing and valuation information with respect to security-based swaps would apply to every security-based swap clearing agency that performs CCP services. As noted above, there are currently four entities providing CCP services for security-based swaps that are authorized to do so pursuant to the CDS Clearing Exemption Orders,[139] and there could conceivably be one or two more entities that clear security-based swaps in the future. Thus, the Commission estimates that four to six clearing agencies that provide CCP services may seek to clear security-based swaps.[140] The Commission is using the higher estimate of six respondent clearing agencies for this PRA analysis.

[135] *See supra* note 6.

[136] *See supra* note 124.

[137] *See supra* note 125.

[138] *See supra* note 134.

[139] *See supra* note 6.

[140] *See supra* note 124 and accompanying text.

5. Clearing Agency Policies and Procedures To Protect the Confidentiality of Trading Information of Clearing Agency Participants

The safeguards and procedures applicable to the confidential treatment of trading information received by a clearing agency under proposed Rule 17Ad–23 would apply to all clearing agencies registered with the Commission. As noted above, there are currently four clearing agencies authorized to clear security-based swaps pursuant to the CDS Clearing Exemption Orders,[141] and there could conceivably be one or two more entities that clear security-based swaps in the future. Thus, the Commission estimates that four to six clearing agencies may seek to clear security-based swaps.[142] The Commission is using the higher estimate of six respondent clearing agencies for this PRA analysis. There are also eleven additional clearing agencies currently registered with the Commission.[143] Thus, for this provision, the Commission estimates that there would be seventeen respondents.[144]

6. Clearing Agency Procedures To Identify and Address Conflicts of Interest

The conflicts of interest policies and procedures to be adopted by clearing agencies pursuant to proposed Rule 17Ad–25 would apply to all clearing agencies registered with the Commission. As noted above, there are currently four clearing agencies authorized to clear security-based swaps pursuant to the CDS Clearing Exemption Orders,[145] and that there could conceivably be one or two more entities that clear security-based swaps in the future. Thus, the Commission estimates that four to six clearing agencies may seek to clear security-based swaps.[146] The Commission is using the higher estimate of six respondent clearing agencies for this PRA analysis. There are also eleven additional clearing agencies currently registered with the Commission.[147] Thus, for this provision, the Commission estimates that there would be seventeen respondents.[148]

7. Standards for Board or Board Committee Directors

The board and board committee directors governance standards to be

[141] *See supra* note 6.

[142] *See supra* note 124 and accompanying text.

[143] *See supra* note 125.

[144] *See supra* note 134.

[145] *See supra* note 6.

[146] *See supra* note 124 and accompanying text.

[147] *See supra* note 125.

[148] *See supra* note 134.

established by clearing agencies pursuant to proposed Rule 17Ad–26 would apply to all clearing agencies registered with the Commission. As noted above, there are currently four clearing agencies authorized to clear security-based swaps pursuant to the CDS Clearing Exemption Orders,[149] and there could conceivably be one or two more entities that clear security-based swaps in the future. Thus, the Commission estimates that four to six clearing agencies may seek to clear security-based swaps.[150] The Commission is using the higher estimate of six respondent clearing agencies for this PRA analysis. There are also eleven additional clearing agencies currently registered with the Commission.[151] Thus, for this provision, the Commission estimates that there would be seventeen respondents.[152]

8. Designation of Chief Compliance Officer

The provisions regarding CCOs of proposed Rule 3Cj–1 would apply to all clearing agencies registered with the Commission. As noted above, there are currently four clearing agencies authorized to clear security-based swaps pursuant to the CDS Clearing Exemption Orders,[153] and there could conceivably be one or two more entities that clear security-based swaps in the future. Thus, the Commission estimates that four to six clearing agencies may seek to clear security-based swaps.[154] The Commission is using the higher estimate of six respondent clearing agencies for this PRA analysis. There are also eleven additional clearing agencies currently registered with the Commission.[155] Thus, for this provision, the Commission estimates that there would be seventeen respondents.[156]

*D. Total Annual Reporting and Recordkeeping Burden*

1. Standards for Clearing Agencies Reporting Requirements

a. Measurement and Management of Credit Exposures

Proposed Rule 17Ad–22(b)(1) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to measure its credit exposures to its participants at least once a day and limit its exposures to potential losses from defaults by its participants in normal market conditions so that the operations of the clearing agency would not be disrupted and non-defaulting participants would not be exposed to losses that they cannot anticipate or control. The exact nature of any rules and procedures a clearing agency would likely establish to support this requirement is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories ("SDRs").[157] Specifically, Rule 611 of Regulation NMS, referred to as the "Order Protection Rule", requires trading centers to establish, maintain, and enforce written policies and procedures that are reasonably designed to prevent trade-throughs on that trading center of protected quotations in NMS stocks, unless an exception applies.[158] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes the requirement for policies and procedures to be created and maintained by SRO and non-SRO trading centers in Rule 611 of Regulation NMS is similar in nature and scope to this requirement for clearing agencies to create policies and procedures.

Accordingly, the Commission believes that the burdens imposed on respondents to create policies and procedures in both contexts would be roughly equivalent. In its adoption of the final Order Protection Rule, the Commission estimated the approximate hourly burdens imposed on trading centers that are SROs and on trading centers that are not SROs to establish written policies and procedures that are reasonably designed to prevent execution of trade-throughs. For SRO trading centers, the Commission estimated that creating written policies and procedures would require approximately 270 hours and require efforts from the various skill sets of the clearing agency's legal, compliance, information technology and business operations personnel. For non-SRO trading centers, the Commission estimated an approximate hourly burden of 210 hours to meet the same requirement. This difference between the hourly burden imposed on non-SRO trading centers and SRO trading centers is primarily due to a slightly lower expectation for the hourly burden imposed on the legal and compliance staff at a non-SRO trading center.

The Commission preliminarily believes that this hourly burden estimate of 210 hours for non-SRO trading centers under Regulation NMS is an appropriate estimate for the burden that would be imposed on clearing agencies to create policies and procedures because, as discussed below, recent assessments of the registered U.S. clearing agencies support the conclusion that clearing agencies and their rule books generally meet or exceed analogous standards of operation and governance to those standards within proposed Rule 17Ad–22.[159] Therefore, those findings and the Commission's experience in oversight of clearing agencies support a preliminary view that the requirements in the rules for clearing agencies proposed by the Commission would in many cases impose a burden on legal and compliance personnel at clearing agencies that would involve adjustments to a registered clearing agency's rule book and its policies and procedures rather than creation of entirely separate policies and procedures to support entirely new operations and practices.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(b)(1) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 1,890 hours.[160] The

[149] *See supra* note 6.

[150] *See supra* note 124 and accompanying text.

[151] *See supra* note 125.

[152] *See supra* note 134.

[153] *See supra* note 6.

[154] *See supra* note 124 and accompanying text.

[155] *See supra* note 125.

[156] *See supra* note 134.

[157] *See* Exchange Act Release Nos. 51808 (June 9, 2005), 70 FR 37496 (June 29, 2005) (discussing in Section VIII.A.4. the time needed from legal, compliance, information technology and business operations personnel to create policies and procedures for preventing and monitoring trade-throughs) and 63347 (November 19, 2010), 75 FR 77306 (December 10, 2010) (discussing in Section V.D.7. the time needed for SDRs to establish and enforce written policies and procedures reasonably designed to minimize conflicts of interest).

[158] *See* 17 CFR 242.611.

[159] *See* infra note 291.

[160] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 9 respondent clearing agencies = 1,890 hours. *See* Exchange Act Release Nos. 51808 (June 9, 2005), 70 FR 37496 (June 29, 2005) (Section VIII.A.4. finding a burden of 210 hours needed for non-SRO trading centers to create one policy and procedure) and 63347 (November 19, 2010), 75 FR 77306 (December 10, 2010) (Section V.D.7. finding a burden of 210 hours needed for an SDR to create one policy and procedure).

Continued

Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies that provide CCP services would be required to measure their credit exposures as required by proposed Rule 17Ad–22(b)(1) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for monitoring custody and investment standards would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 540 hours.[161] The Commission solicits comment regarding the accuracy of this estimate.

b. Margin Requirements

Proposed Rule 17Ad–22(b)(2) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to use margin requirements to limit its credit exposures to participants in normal market conditions and use risk-based models and parameters to set margin requirements and review them at least monthly. The exact nature of any rules and procedures a clearing agency would likely establish to support this requirement is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[162] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(b)(2) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 1,890 hours.[163] The Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies would be required to administer their custody and investment standards required by proposed Rule 17Ad–22(b)(2) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for monitoring custody and investment standards would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 540 hours.[164] The Commission solicits comment regarding the accuracy of this estimate.

c. Financial Resources

Proposed Rule 17Ad–22(b)(3) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to maintain sufficient financial resources to withstand, at a minimum, a default by the participant to which it has the largest exposure in extreme but plausible market conditions, and if the clearing agency provides CCP services for security-based swaps then a default by the two participants to which it has the largest exposures in extreme but plausible market conditions; provided that if a participant controls another participant or is under common control with another participant, the affiliated participant and the participant shall be deemed to be a single participant. The exact nature of any rules and procedures a clearing agency would likely establish to support this requirement is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[165] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(b)(3) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 1,890 hours.[166] The Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies would be required to administer their financial resources standards required by proposed Rule 17Ad–22(b)(3) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for financial resources standards would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing

The Commission based these estimates on the estimates for non-SRO trading centers that appear in Exchange Act Release Nos. 51808 and 63347 because the Commission preliminarily believes that the existing clearing agency requirements under Section 17A of the Exchange Act make these proposed burdens more similar to the less burdensome requirements for non-SRO trading centers than the burdens for SRO trading centers.

[161] This figure was calculated as follows: Compliance Attorney at 60 hours × 9 respondent clearing agencies = 540 hours for all respondent clearing agencies. *See* Exchange Act Release Nos. 51808 (June 9, 2005), 70 FR 37496 (June 29, 2005) (Section VIII.A.4. estimating that it would take the average SRO and non-SRO trading center approximately two hours per month of internal legal time and three hours of internal compliance time to ensure that its written policies and procedures are up-to-date and remain in compliance amounting to an annual burden of 60 hours per year per respondent) and 63347 (November 19, 2010), 75 FR 77306 (December 10, 2010) (Section V.D.7. estimating the time needed for SDRs to establish and enforce written policies and procedures).

[162] *See supra* note 157.

[163] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 9 respondent clearing agencies = 1,890 hours. *See supra* note 160.

[164] This figure was calculated as follows: Compliance Attorney at 60 hours × 9 respondent clearing agencies = 540 hours for all respondent clearing agencies. *See supra* note 161.

[165] *See supra* note 157.

[166] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 9 respondent clearing agencies = 1,890 hours. *See supra* note 160.

agencies of 540 hours.[167] The Commission solicits comment regarding the accuracy of this estimate.

d. Model Validation

As discussed above, proposed Rule 17Ad–22(b)(4) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide for an annual model validation. The Commission preliminarily believes this requirement would help to ensure that a clearing agency's margin model remains effective in determining the appropriate margin level. The exact nature of any rules and procedures a clearing agency would likely establish to support this requirement is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[168] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(b)(4) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 1,890 hours.[169] The Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies would be required to administer their model validation standards required by proposed Rule 17Ad–22(b)(4) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for model validation standards would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 540 hours.[170] The Commission solicits comment regarding the accuracy of this estimate.

Based on its oversight of clearing agencies, the Commission preliminarily estimates that proposed Rule 17Ad–22(b)(4) would impose an annual burden on all respondent clearing agencies of 6,480 hours.[171] The Commission solicits comment regarding the accuracy of this estimate.

e. Non-Dealer Access

Proposed Rule 17Ad–22(b)(5) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide the opportunity for a person that does not perform any dealer or security-based swap dealer services to obtain membership at the clearing agency to clear securities for itself or on behalf of other persons. The exact nature of the procedures a clearing agency would establish to support this requirement is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[172] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(b)(5) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 1,890 hours.[173] The Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies would be required to administer their membership standards required by proposed Rule 17Ad–22(b)(5) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for granting membership to persons that do not perform any dealer or security-based swap dealer services would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 540 hours.[174] The Commission solicits comment regarding the accuracy of this estimate.

f. Portfolio Size and Transaction Volume Thresholds Restrictions

Proposed Rule 17Ad–22(b)(6) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to have membership standards that do not require that participants maintain a portfolio of any minimum size or that participants maintain a minimum transaction volume. The exact nature of the procedures a clearing agency would establish to support this requirement is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[175] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the

[167] This figure was calculated as follows: Compliance Attorney at 60 hours × 9 respondent clearing agencies = 540 hours for all respondent clearing agencies. *See supra* note 161.

[168] *See supra* note 157.

[169] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 9 respondent clearing agencies = 1,890 hours. *See supra* note 160.

[170] This figure was calculated as follows: Compliance Attorney at 60 hours × 9 respondent clearing agencies = 540 hours for all respondent clearing agencies. *See supra* note 161.

[171] This figure was calculated as follows: Consultant at 30 hours per week × 12 weeks × 2 Consultants × 9 respondent clearing agencies = 6,480 hours.

[172] *See supra* note 157.

[173] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 9 respondent clearing agencies = 1,890 hours. *See supra* note 160.

[174] This figure was calculated as follows: Compliance Attorney at 60 hours × 9 respondent clearing agencies = 540 hours for all respondent clearing agencies. *See supra* note 161.

[175] *See supra* note 157.

corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(b)(6) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 1,890 hours.[176] The Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies would be required to administer their membership standards required by proposed Rule 17Ad–22(b)(6) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for not having membership standards that require participants to maintain a portfolio of any minimum size or that participants maintain a minimum transaction volume would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 540 hours.[177] The Commission solicits comment regarding the accuracy of this estimate.

g. Net Capital Requirements

Proposed Rule 17Ad–22(b)(7) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide a person that maintains a net capital equal to or greater than $50 million with the ability to obtain membership at the clearing agency, with any net capital requirements being scalable so that they are proportional to the risks posed by the participant's activities to the clearing agency. The exact nature of the procedures a clearing agency would establish to support this requirement is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[178] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(b)(7) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 1,890 hours.[179] The Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies may need to update these policies and procedures over time, particularly due to the fact that proposed Rule 17Ad–22(b)(7) permits a clearing agency to provide for a higher net capital requirement (*i.e.,* higher than $50 million) as a condition for membership at the clearing agency if the clearing agency demonstrates to the Commission that such a requirement is necessary to mitigate risks that could not otherwise be effectively managed by other measures, such as scalable limitations on the transactions that the participants may clear through the clearing agency, and the Commission approves the higher net capital requirement as part of a rule filing or clearing agency registration application. While the number of times each clearing agency will need to update its policies and procedures to revise its net capital requirements is likely to vary, both over time and between clearing agencies, such changes may occur as a result of an annual review of a clearing agency's operations and default mechanisms. For the same reasons as discussed above, the Commission believes that the estimates of the burden imposed by the policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories[180] are sufficiently similar to serve as a basis for these estimates. Accordingly, the Commission preliminarily estimates that proposed Rule 17Ad–22(b)(7) would impose an annual burden on each respondent clearing agency of 210 hours, corresponding to an aggregate annual burden on all respondent clearing agencies of 1,890 hours.[181] The Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies that provide CCP services would be required to administer their net capital requirements required by proposed Rule 17Ad–22(b)(7) on an ongoing basis. The Commission expects that the exact burden of administering the net capital requirements would vary depending on how frequently each clearing agency providing CCP services may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 540 hours.[182] The Commission solicits comment regarding the accuracy of this estimate.

h. Record of Financial Resources

As detailed above, pursuant to proposed Rule 17Ad–22(c)(1), clearing agencies that perform central counterparty services would be required each fiscal quarter (based on calculations made as of the last business day of the clearing agency's fiscal quarter), or at any time upon Commission request, to calculate and maintain a record of the financial resources necessary to meet the requirement in proposed Rule 17Ad–22(c)(1) and sufficient documentation to explain the methodology it uses to compute such financial resource requirement.

The exact nature of the procedures a clearing agency would establish to support this requirement is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation

[176] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 9 respondent clearing agencies = 1,890 hours. *See supra* note 160.

[177] This figure was calculated as follows: Compliance Attorney at 60 hours × 9 respondent clearing agencies = 540 hours for all respondent clearing agencies. *See supra* note 161.

[178] *See supra* note 157.

[179] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × nine respondent clearing agencies = 1,890 hours. *See supra* note 160.

[180] *See supra* note 157.

[181] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × nine respondent clearing agencies = 1,890 hours. *See supra* note 160.

[182] This figure was calculated as follows: Compliance Attorney at 60 hours × 9 respondent clearing agencies = 540 hours for all respondent clearing agencies. *See supra* note 161.

NMS and in proposed requirements for security-based swap data repositories.[183] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(c)(1) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 1,890 hours.[184] The Commission solicits comment regarding the accuracy of this estimate.

Based on its oversight of clearing agencies, the Commission believes that the respondent clearing agencies already have methodologies designed to ensure that in providing CCP services the clearing agency can withstand a default by the participant to which the clearing agency has the largest exposure in extreme but plausible market conditions.[185] Because clearing agencies that provide CCP services already use such methodologies, the Commission preliminarily believes the one-time burden imposed would involve adjustments needed to synthesize and format existing information in a manner sufficient to explain the methodology the clearing agency uses to meet the requirement of proposed Rule 17Ad–22(c)(1). The Commission preliminarily believes these adjustments would impose a one-time burden of 100 hours on each clearing agency, corresponding to an aggregate one-time burden imposed on all clearing agencies of 900 hours.[186] The Commission solicits comment regarding the accuracy of this estimate.

On an ongoing basis, the Commission estimates that for a clearing agency to generate the required reports concerning its financial resources would impose a burden of three hours per respondent clearing agency per quarter. This amounts to an annual burden of 12 hours for each clearing agency and corresponds to an aggregate annual burden of 108 hours for all respondent clearing agencies.[187] The Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies providing CCP services would also be required to administer any procedures used to support compliance with Rule 17Ad–22(c)(1) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for granting membership to persons that do not perform any dealer or security-based swap dealer services would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 540 hours.[188] The Commission solicits comment regarding the accuracy of this estimate.

i. Annual Audited Financial Report

Proposed Rule 17Ad–22(c)(2) would also require that a clearing agency post on its Web site an annual financial report. Each financial report shall (i) be a complete set of financial statements of the clearing agency for the most recent two fiscal years and be prepared in accordance with U.S. GAAP, except that for a clearing agency that is a corporation or other organization incorporated or organized under the laws of any foreign country the financial statements may be prepared according to U.S. GAAP or IFRS; (ii) be audited in accordance with standards of the Public Company Accounting Oversight Board by a registered public accounting firm that is qualified and independent in accordance with Rule 2–01 of Regulation S–X; and (iii) include report of the registered public accounting firm that complies with paragraphs (a) through (d) of Rule 2–02 of Regulation S–X.

The exact nature of the procedures a clearing agency would establish to support this requirement is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[189] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(c)(2) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 3,570 hours.[190] The Commission solicits comment regarding the accuracy of this estimate.

The Commission preliminarily believes, based on its oversight of clearing agencies, that the one-time burden imposed by the rule would involve systems adjustments at the clearing agency needed to facilitate posting of the annual audited financial report to the clearing agency's Web site. The Commission preliminarily believes these adjustments would impose a one-time burden of 100 hours on each clearing agency, corresponding to an aggregate one-time burden imposed on

[183] *See supra* note 157.

[184] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 9 respondent clearing agencies = 1,890 hours. *See supra* note 160.

[185] *See, e.g.,* International Monetary Fund, *Publication of Financial Sector Assessment Program Documentation—Detailed Assessment of Observance of the National Securities Clearing Corporation's Observance of the CPSS–IOSCO Recommendations for Central Counterparties,* 10 (2010) (assessing National Securities Clearing Corporation's observance of Recommendation 5 from the RCCP that a CCP should maintain sufficient financial resources to withstand, at a minimum, the default of a participant to which it has the largest exposure in extreme but plausible market conditions and noting that NSCC began evaluating itself against this standard in 2009 and has back-testing results to support that during the period from January through April 2009 there was sufficient liquidity to cover the needs of the failure of the largest affiliated family 99.98 percent of the time), *available at http://www.imf.org/external/pubs/ft/scr/2010/cr10129.pdf.*

[186] This figure was calculated as follows: ((Chief Compliance Officer at 40 hours) + (Computer Operations Department Manager at 40 hours) + (Senior Programmer at 20 hours)) = 100 hours × 9 respondent clearing agencies = 900 hours. *See infra* note 253 and accompanying text.

[187] This figure was calculated as follows: ((Compliance Attorney at 1 hour) + (Computer Operations Department Manager at 2 hours)) = 3 hours per quarter × 4 quarters per year = 12 hours per year × 9 respondent clearing agencies = 108 hours.

[188] This figure was calculated as follows: Compliance Attorney at 60 hours × 9 respondent clearing agencies = 540 hours for all respondent clearing agencies. *See supra* note 161.

[189] *See supra* note 157.

[190] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 17 respondent clearing agencies = 3,570 hours. *See supra* note 160.

all clearing agencies of 1,700 hours.[191] The Commission solicits comment regarding the accuracy of this estimate.

On an ongoing basis, clearing agencies would be required to administer any policies and procedures used to support compliance with Rule 17Ad–22(c)(2). The Commission expects that the exact burden of administering the procedures for facilitating an annual audit report of the clearing agency and posting that annual audit report to the clearing agency's Web site would vary. However, based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 1,020 hours.[192] The Commission solicits comment regarding the accuracy of this estimate.

The Commission estimates based on its experience with entities of similar size to the respondents to this collection, that these reports would generally require on average 500 hours annually per respondent clearing agency to generate and cost $500,000 for independent public accounting services. Thus, the Commission preliminarily believes this corresponds to an aggregate annual burden to all clearing agencies of 8,500 hours and $8,500,000.[193] The Commission solicits comment as to the accuracy of this estimate.

j. Transparent and Enforceable Rules and Procedures

Proposed Rule 17Ad–22(d)(1) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide for a well founded, transparent and enforceable legal framework. The exact nature of the policies and procedures a clearing agency would establish is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for SDRs.[194] Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(d)(1) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 3,570 hours.[195] The Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies would be required to administer their rules and procedures to ensure they provide for a well founded, transparent and enforceable legal framework on an ongoing basis. The Commission expects that the exact burden of administering the procedures for monitoring participation standards would vary depending on how frequently each clearing agency may need to update its rules and procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 1,020 hours.[196] The Commission solicits comment regarding the accuracy of this estimate.

k. Participation Requirements

Proposed Rule 17Ad–22(d)(2) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to have procedures in place to monitor that their participation requirements are met on an ongoing basis. The exact nature of the procedures a clearing agency would establish is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[197] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(d)(2) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 3,570 hours.[198] The Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies would be required to administer their participation requirements required by proposed Rule 17Ad–22(d)(2) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for monitoring participation requirements would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 1,020 hours.[199] The Commission solicits comment regarding the accuracy of this estimate.

Additionally, proposed Rule 17Ad–22(d)(2) would require clearing agencies to publicly disclose their participation requirements. Based on staff discussions with respondents that are already subject to a similar requirement in the CDS Clearing Exemption Orders to make publicly available certain pricing and

[191] This figure was calculated as follows: ((Chief Compliance Officer at 40 hours) + (Computer Operations Department Manager at 40 hours) + (Senior Programmer at 20 hours)) = 100 hours × 9 respondent clearing agencies = 900 hours. *See infra* note 253 and accompanying text.

[192] This figure was calculated as follows: Compliance Attorney at 60 hours × 17 respondent clearing agencies = 1,020 hours for all respondent clearing agencies. *See supra* note 161.

[193] *See* Exchange Act Release No. 63347 (November 19, 2010), 75 FR 77306 (December 10, 2010) (Section VI.F.2. discussing the time the Commission preliminarily estimates an SDR would need to prepare and file annual financial reports with the Commission pursuant to proposed Rule 13n–11(f) and (g)). This figure was calculated as follows: Senior Accountant at 500 hours × 17 respondent clearing agencies = 8,500 hours.

[194] *See supra* note 157.

[195] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours) = 210 hours × 17 respondent clearing agencies = 3,570 hours.

[196] This figure was calculated as follows: Compliance Attorney at 60 hours × 17 respondent clearing agencies = 1,020 hours.

[197] *See supra* note 157.

[198] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 17 respondent clearing agencies = 3,570 hours. *See supra* note 195.

[199] This figure was calculated as follows: Compliance Attorney at 60 hours × 17 respondent clearing agencies = 1,020 hours. *See supra* note 196.

valuation information for security-based swaps,[200] the Commission estimates that the one-time burden for a security-based swap clearing agency to comply with the requirements of proposed Rule 17Ad–22(d)(2) would involve slight adjustments to computer data systems that would already be in place as part of its clearing agency operations under Exchange Act Section 17A. The Commission preliminarily believes that a similar analysis would apply to each of the other registered clearing agencies. Therefore, the Commission does not anticipate that new hardware, such as additional computer equipment, would be required. Instead, the Commission broadly estimates that a clearing agency's adjustments to its systems to meet the requirements of proposed Rule 17Ad–22(d)(2) would impose a one-time burden of 100 hours on each respondent clearing agency, corresponding to an aggregate one-time burden imposed on all respondent clearing agencies of 1,700 hours.[201] The Commission solicits comment regarding the accuracy of this estimate.

Respondent clearing agencies would also have an ongoing responsibility to make their participation requirements available. Also based on staff discussion with respondents that are already subject to the requirement in the CDS Clearing Exemption Orders to make certain pricing and valuation information publicly available, the Commission preliminarily believes that the ongoing burden would be limited and would likely involve maintenance and troubleshooting of computer systems used to facilitate dissemination of participant requirements. Therefore, the Commission preliminarily estimates this would impose an annual aggregate burden of 60 hours for each respondent clearing agency, which corresponds to an ongoing aggregate annual burden of 1,020 hours for all respondent clearing agencies.[202] The Commission solicits comment regarding the accuracy of this estimate.

l. Identification and Mitigation of Custody of Assets and Investment Risk

Proposed Rule 17Ad–22(d)(3) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to hold assets in a manner that minimizes risk of loss or delay in access to them, and to invest assets in instruments with minimal credit, market, and liquidity risks. The exact nature of any rules and procedures a clearing agency would likely establish to support this requirement is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[203] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(d)(3) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 3,570 hours.[204] The Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies would be required to administer their custody and investment standards required by proposed Rule 17Ad–22(d)(3) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for monitoring custody and investment standards would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 1,020 hours.[205] The Commission solicits comment regarding the accuracy of this estimate.

m. Identification and Mitigation of Operational Risk

Proposed Rule 17Ad–22(d)(4) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to identify and have procedures in place, including business continuity plans, to minimize sources of operational risk. The exact nature of the procedures a clearing agency would establish is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[206] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(d)(4) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 3,570 hours.[207] The Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies would be required to administer their operational standards required by proposed Rule 17Ad–22(d)(4) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for monitoring operational risks would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours

[200] *See infra* notes 251–254 and accompanying text.

[201] This figure was calculated as follows: ((Chief Compliance Officer at 40 hours) + (Computer Operations Department Manager at 40 hours) + (Senior Programmer at 20 hours)) = 100 hours × 17 respondent clearing agencies = 1,700 hours. *See infra* note 253 and accompanying text.

[202] This figure was calculated as follows: Computer Operations Department Manager at 60 hours annually × 17 respondent clearing agencies = 1,020 hours for all respondent clearing agencies. *See supra* note 196.

[203] *See supra* note 157.

[204] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 17 respondent clearing agencies = 3,570 hours. *See supra* note 195.

[205] This figure was calculated as follows: Compliance Attorney at 60 hours × 17 respondent clearing agencies = 1,020 hours for all respondent clearing agencies. *See supra* note 196.

[206] *See supra* note 157.

[207] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 17 respondent clearing agencies = 3,570 hours. *See supra* note 195.

on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 1,020 hours.[208] The Commission solicits comment regarding the accuracy of this estimate.

n. Money Settlement Risks

Proposed Rule 17Ad–22(d)(5) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to employ money settlement arrangements that eliminate or strictly limit the clearing agency's settlement bank risks, that is, its credit and liquidity risks from the use of banks to effect money settlements with its participants; and require funds transfers to the clearing agency to be final when effected. The exact nature of any rules and procedures a clearing agency would likely establish to support this requirement is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[209] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(d)(5) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 3,570 hours.[210] The Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies would be required to administer their settlement arrangements required by proposed Rule 17Ad–22(d)(5) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for monitoring settlement arrangements would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 1,020 hours.[211] The Commission solicits comment regarding the accuracy of this estimate.

o. Cost-Effectiveness

Proposed Rule 17Ad–22(d)(6) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to be cost effective in meeting the requirements of participants while maintaining safe and secure operations. The exact nature of any rules and procedures a clearing agency would likely establish to support this requirement is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[212] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(d)(6) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 3,570 hours.[213] The Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies would be required to administer their cost-effectiveness standards required by proposed Rule 17Ad–22(d)(6) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for monitoring cost-effectiveness standards would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 1,020 hours.[214] The Commission solicits comment regarding the accuracy of this estimate.

p. Links

Proposed Rule 17Ad–22(d)(7) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to evaluate the potential sources of risks that can arise when the clearing agency establishes links either cross-border or domestically to clear trades and ensure that the risks are managed prudently on an ongoing basis. The exact nature of any rules and procedures a clearing agency would likely establish to support this requirement is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[215] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(d)(7) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time

[208] This figure was calculated as follows: Compliance Attorney at 60 hours × 17 respondent clearing agencies = 1,020 hours for all respondent clearing agencies. *See supra* note 196.

[209] *See supra* note 157.

[210] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 17 respondent clearing agencies = 3,570 hours. *See supra* note 195.

[211] This figure was calculated as follows: Compliance Attorney at 60 hours × 17 respondent clearing agencies = 1,020 hours for all respondent clearing agencies. *See supra* note 196.

[212] *See supra* note 157.

[213] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 17 respondent clearing agencies = 3,570 hours. *See supra* note 195.

[214] This figure was calculated as follows: Compliance Attorney at 60 hours × 17 respondent clearing agencies = 1,020 hours for all respondent clearing agencies. *See supra* note 196.

[215] *See supra* note 157.

burden on all respondent clearing agencies of 3,570 hours.[216] The Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies would be required to administer their links arrangements as required by proposed Rule 17Ad–22(d)(7) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for monitoring links arrangements would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 1,020 hours.[217] The Commission solicits comment regarding the accuracy of this estimate.

q. Governance

Proposed Rule 17Ad–22(d)(8) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to have governance arrangements that are clear and transparent to fulfill the public interest requirements in Section 17A of the Act applicable to clearing agencies, to support the objectives of owners and participants, and to promote the effectiveness of the clearing agency's risk management procedures. The exact nature of any rules and procedures a clearing agency would likely establish to support this requirement is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[218] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(d)(8) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 3,570 hours.[219] The Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies would be required to administer their governance arrangements as required by proposed Rule 17Ad–22(d)(8) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for monitoring governance arrangements would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 1,020 hours.[220] The Commission solicits comment regarding the accuracy of this estimate.

Based on information from respondents that are already subject to a similar requirement in the CDS Clearing Exemption Orders to make publicly available certain pricing and valuation information with respect to security-based swaps,[221] the Commission estimates that the one-time burden for a clearing agency to provide transparency about its governance arrangements to fulfill the public interest requirements in Section 17A of the Exchange Act would involve slight adjustments to data systems that would already be in place as part of the clearing agency's operations. Therefore, the Commission does not anticipate that new hardware, such as additional computer equipment, would be required. Instead, the Commission broadly estimates that for a clearing agency to adjust its systems to meet the requirements of proposed Rule 17Ad–22(d)(8) would impose a one-time burden of 100 hours on each respondent clearing agency, corresponding to an aggregate one-time burden imposed on all respondent clearing agencies of 1,700 hours.[222] The Commission solicits comment regarding the accuracy of this estimate.

r. Information on Services

Proposed Rule 17Ad–22(d)(9) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide market participants with sufficient information for them to identify and evaluate the risks and costs associated with using their services. The exact nature of any rules and procedures a clearing agency would likely establish to support this requirement is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[223] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(d)(9) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 3,570 hours.[224] The Commission solicits comment regarding the accuracy of this estimate.

[216] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 17 respondent clearing agencies = 3,570 hours. *See supra* note 195.

[217] This figure was calculated as follows: Compliance Attorney at 60 hours × 17 respondent clearing agencies = 1,020 hours for all respondent clearing agencies. *See supra* note 196.

[218] *See supra* note 157.

[219] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 17 respondent clearing agencies = 3,570 hours. *See supra* note 195.

[220] This figure was calculated as follows: Compliance Attorney at 60 hours × 17 respondent clearing agencies = 1,020 hours for all respondent clearing agencies. *See supra* note 196.

[221] *See infra* notes 251–254 and accompanying text.

[222] This figure was calculated as follows: ((Chief Compliance Officer at 40 hours) + (Computer Operations Department Manager at 40 hours) + (Senior Programmer at 20 hours)) × 17 respondent clearing agencies = 1,700 hours. *See infra* note 253 and accompanying text.

[223] *See supra* note 157.

[224] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 17 respondent clearing agencies = 3,570 hours. *See supra* note 195.

Respondent clearing agencies would also have an ongoing responsibility to make this information available. Also based on informal comments from respondents already subject to a similar requirement in the CDS Clearing Exemption Orders to make certain pricing and valuation information with respect to security-based swaps publicly available, the Commission preliminarily believes that the ongoing burden would be limited and would likely involve maintenance and troubleshooting of computer systems used to facilitate dissemination of information responsive to Rule 17Ad–22(d)(9). Therefore, the Commission preliminarily estimates this would impose an annual aggregate burden of 60 hours for each respondent clearing agency, which corresponds to an ongoing aggregate annual burden of 1,020 hours for all respondent clearing agencies.[225] The Commission solicits comment regarding the accuracy of this estimate.

Based on information from respondents that are already subject to a similar requirement in the CDS Clearing Exemption Orders to make publicly available certain pricing and valuation information with respect to security-based swaps,[226] the Commission estimates that the one-time burden to provide market participants with sufficient information for them to identify and evaluate accurately the risks and costs associated with using a clearing agency's services would involve slight adjustments to data systems that would already be in place as part of the clearing agency's operations under Exchange Act Section 17A. Therefore, the Commission does not anticipate that new hardware, such as additional computer equipment, would be required. Instead, the Commission broadly estimates that for a clearing agency to adjust its systems to meet the requirements of proposed Rule 17Ad–22(d)(9) would impose a one-time burden of 100 hours on each respondent clearing agency, corresponding to an aggregate one-time burden imposed on all respondent clearing agencies of 1,700 hours.[227] The Commission solicits comment regarding the accuracy of this estimate.

s. Immobilization and Dematerialization of Stock Certificates

Proposed Rule 17Ad–22(d)(10) would require clearing agencies that provide central securities depository services to establish, implement, maintain and enforce written policies and procedures reasonably designed to immobilize or dematerialize securities certificates and transfer them by book entry to the greatest extent possible. The exact nature of any rules and procedures a clearing agency would likely establish to support this requirement is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[228] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17AAd–22d)(10) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 3,570 hours.[229] The Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies that provide central securities depository services would be required to administer their standards for immobilizing or dematerializing securities certificates as required by proposed Rule 17AAd–22d)(10) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for immobilizing and dematerializing securities certificates would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 1020 hours.[230] The Commission solicits comment regarding the accuracy of this estimate.

t. Default Procedures

Proposed Rule 17AAd–22d)(11) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to make key aspects of the clearing agency's default procedures publicly available and to establish default procedures that ensure that the clearing agency can take timely action to contain losses and liquidity pressures and to continue meeting its obligations in the event of a participant default. The exact nature of the procedures a clearing agency would establish is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[231] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17AAd–22d)(11) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 3,570 hours.[232]

Clearing agencies would be required to administer their default standards required by proposed Rule 17AAd–22d)(11) on an ongoing basis. The Commission expects that the exact burden of administering the procedures

[225] This figure was calculated as follows: Computer Operations Department Manager at 60 hours annually × 17 respondent clearing agencies = 1,020 hours for all respondent clearing agencies. *See supra* note 196.

[226] *See infra* notes 251–254 and accompanying text.

[227] This figure was calculated as follows: ((Chief Compliance Officer at 40 hours) + (Computer Operations Department Manager at 40 hours) + (Senior Programmer at 20 hours)) × 17 respondent clearing agencies = 1,700 hours. *See infra* note 253 and accompanying text.

[228] *See supra* note 157.

[229] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 17 respondent clearing agencies = 3,570 hours. *See supra* note 195.

[230] This figure was calculated as follows: Compliance Attorney at 60 hours × 17 respondent clearing agency = 1020 hours for all respondent clearing agencies. *See supra* note 196.

[231] *See supra* note 157.

[232] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 17 respondent clearing agencies = 3,570 hours. *See supra* note 195.

for monitoring default standards would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 1,020 hours.[233] The Commission solicits comment regarding the accuracy of this estimate.

Based on information from respondents that are already subject to a similar requirement in the CDS Clearing Exemption Orders to make publicly available certain pricing and valuation information with respect to security-based swaps,[234] the Commission estimates that the one-time burden for a clearing agency to make key aspects of its default procedures publicly available would involve slight adjustments to data systems that would already be in place as part of the clearing agency's operations under Section 17A of the Exchange Act. Therefore, the Commission does not anticipate that new hardware, such as additional computer equipment, would be required. Instead, the Commission broadly estimates that for a clearing agency to adjust its systems to meet the requirements of proposed Rule 17AAd–22d)(11) would impose a one-time burden of 100 hours on each respondent clearing agency, corresponding to an aggregate one-time burden imposed on all respondent clearing agencies of 1,700 hours.[235] The Commission solicits comment regarding the accuracy of this estimate.

u. Timing of Settlement Finality

Proposed Rule 17Ad–22(d)(12) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to ensure that final settlement occurs no later than the end of the settlement day and require that intraday or real-time finality be provided where necessary to reduce risks. The exact nature of the procedures a clearing agency would establish is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories. While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(d)(12) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 3,570 hours.[236]

Clearing agencies would be required to administer their settlement finality standards required by proposed Rule 17Ad–22(d)(12) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for ensuring the timing of settlement finality would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 1,020 hours.[237] The Commission solicits comment regarding the accuracy of this estimate.

v. Delivery Versus Payment

Proposed Rule 17Ad–22(d)(13) would require clearing agencies to establish, implement, maintain and enforce written policies and procedures reasonably designed to eliminate principal risk by linking securities transfers to funds transfers in a way that achieves delivery versus payment. The exact nature of the procedures a clearing agency would establish is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[238] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(d)(13) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 3,570 hours.[239]

Clearing agencies would be required to administer their delivery versus payment standards required by proposed Rule 17Ad–22(d)(13) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for delivery versus payment would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 1,020 hours.[240] The Commission solicits comment regarding the accuracy of this estimate.

w. Risk Controls To Address Participants' Failure To Settle

Proposed Rule 17Ad–22(d)(14) would require clearing agencies to establish, implement, maintain and enforce

[233] This figure was calculated as follows: Compliance Attorney at 60 hours × 17 respondent clearing agencies = 1,020 hours. *See supra* note 196.

[234] *See infra* notes 251–254 and accompanying text.

[235] This figure was calculated as follows: ((Chief Compliance Officer at 40 hours) + (Computer Operations Department Manager at 40 hours) + (Senior Programmer at 20 hours)) × 17 respondent clearing agencies = 1,700 hours. *See infra* note 253 and accompanying text.

[236] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 17 respondent clearing agencies = 3,570 hours. *See supra* note 195.

[237] This figure was calculated as follows: Compliance Attorney at 60 hours × 17 respondent clearing agencies = 1,020 hours. *See supra* note 196.

[238] *See supra* note 157.

[239] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 17 respondent clearing agencies = 3,570 hours. *See supra* note 195.

[240] This figure was calculated as follows: Compliance Attorney at 60 hours × 17 respondent clearing agencies = 1,020 hours. *See supra* note 196.

written policies and procedures reasonably designed to institute risk controls, including collateral requirements and limits to cover the clearing agency's credit exposure to each participant exposure fully, and that ensure timely settlement in the event that the participant with the largest payment obligation is unable to settle when the clearing agency provides central securities depository services and extends intraday credit to participants. The exact nature of any rules and procedures a clearing agency would likely establish to support this requirement is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[241] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(d)(14) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 3,570 hours.[242] The Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies that provide central securities depository services would be required to administer their risk control standards required by proposed Rule 17Ad–22(d)(14) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for risk controls, including collateral requirements and limits to cover the clearing agency's credit exposure to each participant exposure fully and that ensure timely settlement in the event that the participant with the largest payment obligation is unable to settle would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 1,020 hours.[243] The Commission solicits comment regarding the accuracy of this estimate.

x. Identification and Management of Physical Delivery Risks

Proposed Rule 17Ad–22(d)(15) would require a clearing agency to state to its participants the clearing agency's obligations with respect to physical deliveries and to identify and manage the risks that arise in connection with these obligations. The exact form in which a clearing agency would state to its participants the clearing agency's obligations with respect to physical deliveries and to identify and manage the risks in connection with those obligations is likely to vary between clearing agencies. However, there are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[244] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–22(d)(15) would impose a one-time burden on each respondent clearing agency of 210 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 3,570 hours.[245] The Commission solicits comment regarding the accuracy of this estimate.

Clearing agencies would be required to administer their physical delivery standards required by proposed Rule 17Ad–22(d)(15) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for monitoring physical delivery standards would vary depending on how frequently each clearing agency may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 1,020 hours.[246] The Commission solicits comment regarding the accuracy of this estimate.

Based on information from respondents that are already subject to a similar requirement in the CDS Clearing Exemption Orders to make publicly available certain pricing and valuation information with respect to security-based swaps,[247] the Commission estimates that the one-time burden for a clearing agency to state to its participants its obligations with respect to physical deliveries would involve slight adjustments to data systems that would already be in place as part of the clearing agency's operations under Section 17A of the Exchange Act. Therefore, the Commission does not anticipate that new hardware, such as additional computer equipment, would be required. Instead, the Commission broadly estimates that for a clearing agency to adjust its systems to meet the requirements of proposed Rule 17Ad–22(d)(15) would impose a one-time burden of 100 hours on each respondent clearing agency, corresponding to an aggregate one-time burden imposed on all respondent clearing agencies of 1,700 hours.[248] The Commission solicits comment regarding the accuracy of this estimate.

Total Burden

The Commission preliminarily believes that for all respondent clearing agencies the aggregate paperwork burdens contained in proposed Rules

[241] *See supra* note 157.

[242] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 17 respondent clearing agencies = 3,570 hours. *See supra* note 195.

[243] This figure was calculated as follows: Compliance Attorney at 60 hours × 17 respondent clearing agencies = 1,020 hours for all respondent clearing agencies. *See supra* note 196.

[244] *See supra* note 157.

[245] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 17 respondent clearing agencies = 3,570 hours. *See supra* note 195.

[246] This figure was calculated as follows: Compliance Attorney at 60 hours × 17 respondent clearing agencies = 1,020 hours. *See supra* note 196.

[247] *See infra* notes 251–254 and accompanying text.

[248] This figure was calculated as follows: ((Chief Compliance Officer at 40 hours) + (Computer Operations Department Manager at 40 hours) + (Senior Programmer at 20 hours)) × 17 respondent clearing agencies = 1,700 hours. *See infra* note 253 and accompanying text.

17Ad–22(d)(1), (2), (3), (4), (5), (6), (7), (8), (9), (10), (11), (12), (13), (14), (15), (b)(1), (2), (3), (4), (5), (6), (7), (c)(1) and (2) would impose a one-time burden of 83,343 hours [249] and an ongoing annual burden of 39,658 hours.[250] The Commission solicits comment regarding the accuracy of this estimate.

2. Dissemination of Pricing and Valuation Information by Security-Based Swap Clearing Agencies That Perform Central Counterparty Services

The requirement for dissemination of pricing and valuation information in proposed Rule 17Aj–1 would effectively require each of the entities authorized to provide CCP services for security-based swaps pursuant to the CDS Clearing Exemption Orders [251] to continue the information dissemination practices they already perform. These entities generate end of day settlement prices and other model prices for security-based swaps, which can be used to establish margin requirements for participant positions and could provide prices in the event of a default scenario. As outlined above, the Commission estimates a total of six respondents would be subject to this requirement.[252]

Based on information from respondents that are already subject to a similar requirement in the CDS Clearing Exemption Orders to disseminate pricing and valuation information, the Commission preliminarily believes that the requirements of proposed Rule 17Aj–1 would impose one-time and ongoing burdens on respondent clearing agencies. For instance, compliance professionals may need to work with information technology and operations professionals to accurately memorialize in writing the specific policy and procedure requirements regarding the dissemination of pricing and valuation information. Information technology personnel may be relied on to develop or modify computer programs that facilitate the requirements of the policies and procedures.

The Commission estimates that the one-time burden for a security-based swap clearing agency to comply with the requirements of proposed Rule 17Aj–1 would involve slight adjustments to data systems that would already be in place as part of the operation of the respondent as a registered clearing agency that provides CCP services for security-based swaps. Therefore, the Commission does not anticipate that new hardware, such as additional computer equipment, would be required. Instead, the Commission broadly estimates that for a clearing agency to adjust its systems to meet the requirements of proposed Rule 17Aj–1 would impose a one-time burden of 100 hours on each respondent clearing agency, corresponding to an aggregate one-time burden imposed on all respondent clearing agencies of 600 hours.[253] The Commission solicits comment regarding the accuracy of this estimate.

Respondent clearing agencies would also have an ongoing responsibility to make their relevant pricing and valuation information available. Based on informal comments from respondents that are already subject to a similar requirement in the CDS Clearing Exemption Orders, the Commission preliminarily believes that the ongoing burden would be limited and would likely involve maintenance and troubleshooting of computer systems used to facilitate dissemination of covered pricing and valuation information. Therefore, the Commission preliminarily estimates this would impose an annual aggregate burden of 60 hours for each respondent clearing agency, which corresponds to an ongoing aggregate annual burden of 360 hours for all respondent clearing agencies.[254] The Commission solicits comment regarding the accuracy of this estimate.

3. Clearing Agency Policies and Procedures To Protect the Confidentiality of Trading Information of Clearing Agency Participants

Proposed Rule 17Ad–23 would require each clearing agency to establish, maintain and enforce written policies and procedures designed to protect the confidentiality of clearing members' trading information. As outlined above, the Commission estimates a total of 17 respondents to this requirement.[255]

Based on the staff's conversations with respondents that are already subject to a similar policies and procedures requirement as part of the CDS Clearing Exemption Orders, the Commission preliminarily believes that establishing, maintaining and enforcing written policies and procedures to protect confidential information of clearing members would require collaboration and coordination across business units within the clearing agency. For instance, legal or compliance professionals may need to work with information technology and operations professionals to accurately memorialize in writing the specific policy and procedure requirements that the clearing agency decides to establish. Information technology personnel may be heavily relied on to develop or modify computer programs that facilitate the requirements of the policies and procedures. Developing business practices that are synchronized with the policies and procedures may also entail coordination with the clearing agency's human resources or risk management personnel to ensure effective adoption of any employee training created to inform employees about trading restrictions or other areas of the policies and procedures that impact them.

The exact nature of the written policies and procedures a clearing agency would establish is likely to vary. However, based on preliminary

[249] This figure combines the one-time burdens for proposed Rules 17Ad–22(d)(1), (2), (3), (4), (5), (6), (7), (8), (9), (10), (11), (12), (13), (14), (15), (b)(1), (2), (3), (4), (5), (6), (7), (c)(1) and (2) and was calculated as follows: (((3,570 hours × 16 standards pursuant to proposed Rules 17Ad–22(d)(1), (2), (3), (4), (5), (6), (7), (8), (9), (10), (11), (12), (13), (14), (15) and (d)(2) = 57,123 hours) + (1,890 hours × 8 standards pursuant to proposed Rules 17Ad–22(b)(1), (2), (3), (4), (5), (6), (7) and (d)(1) = 15,120 hours) + (1,700 hours × 6 systems adjustments pursuant to Rules 17Ad–22(d)(2), (8), (9), (11), (15), (d)(2) = 10,200 hours) + (900 hours × 1 systems adjustment pursuant to Rule 17Ad–22(c)(1)) = 83,343 hours.

[250] This figure combines the annual burdens for proposed Rules 17Ad–22(d)(1), (2), (3), (4), (5), (6), (7), (8), (9), (10), (11), (12), (13), (14), (15), (b)(1), (2), (3), (4), (5), (6), (7), (c)(1) and (2) and was calculated as follows: ((1,020 hours × 16 standards to be administered pursuant to Rules 17Ad–22(d)(1), (2), (3), (4), (5), (6), (7), (8), (9), (10), (11), (12), (13), (14), (15) and (d)(2) = 16,320 hours) + (540 hours × 8 standards to be administered pursuant to proposed Rules 17Ad–22(b)(1), (2), (3), (4), (5), (6), (7) and (d)(1) = 4,320 hours) + (1,020 hours × 2 ongoing efforts to maintain and troubleshoot computer systems used to facilitate dissemination of information responsive to Rules 17Ad–22(d)(2) and (9) = 2,040 hours) + (6,480 hours to prepare the annual model validation required pursuant to Rule 17Ad–22(b)(4)) + (1,890 hours to prepare revised policies and procedures providing for a higher net capital requirement pursuant to Rule 17Ad–22(b)(7) + (108 hours to generate the financial information required pursuant to Rule 17Ad–22(c)(1)) + (8,500 hours to coordinate the posting of financial information to the clearing agency's Web site as required pursuant to Rule 17Ad–22(c)(2)) = 39,658 hours.

[251] *See supra* note 6.

[252] *See supra* notes 139–140 and accompanying text. The Commission notes that clearing agencies operating under the existing CDS Clearing Exemption Orders may not need to make additional changes to meet the requirements of the proposed rule because they are already subject to similar conditions as part of the orders. However, for purposes of this PRA analysis the Commission assumes that these would be new requirements.

[253] This figure was calculated as follows: ((Chief Compliance Officer at 40 hours) + (Computer Operations Department Manager at 40 hours) + (Senior Programmer at 20 hours)) = 100 hours × 6 respondent clearing agencies = 600 hours.

[254] This figure was calculated as follows: Computer Operations Department Manager at 60 hours annually × 6 respondent clearing agencies = 360 hours.

[255] *See supra* notes 141–144 and accompanying text.

information from respondents that are affected by similar requirements under the CDS Clearing Exemption Orders and also based on the Commission's experience in administering those orders, the Commission preliminarily believes that the proposed rule would impose a one-time burden on each respondent clearing agency of 610 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 10,370 hours.[256] The Commission solicits comment regarding the accuracy of this estimate.

Also based on information from respondents that have been subject to the CDS Clearing Exemption Orders, the Commission preliminarily believes that a clearing agency would likely purchase computer software from a third party vendor that the clearing agency would then use to implement the aspects of its policies and procedures designed to restrict, as appropriate, the trading of clearing agency employees for their own account and to prevent misuse and misappropriation of participant information protected by the rule. The cost of such computer software is likely to vary according to the specific policies and procedures of the clearing agency (*i.e.,* based on the number of licenses it may need to cover its employees, the types of services it needs the software to provide, *etc.*). However the Commission preliminarily estimates that the rule would impose a one-time cost of approximately $10,000 dollars on each clearing agency, corresponding to an aggregate one-time burden on all clearing agencies of $170,000.[257] The Commission solicits comment regarding the accuracy of this estimate.

The Commission also preliminarily understands from respondents subject to the similar requirement in the CDS Clearing Exemption Orders that monitoring and enforcing the written policies and procedures required by proposed Rule 17Ad–23 would likely require resource commitments from many of the same business units needed to develop such policies and procedures. For instance, as part of the effort to restrict, as appropriate, trading by clearing agency employees for their own accounts and to prevent misuse and misappropriation of information protected by the rule, the Commission preliminarily believes a clearing agency would need to devote fifty percent of the work hours of a full-time, compliance attorney. The Commission preliminarily expects this resource commitment may, among other things, take the form of obtaining and reviewing brokerage statements of clearing agency employees and reviewing their e-mails. Time for employee training related to the requirements of the policies and procedures, troubleshooting any computer systems designed to protect information in connection with the policies and procedures, and amendments to the policies and procedures are also factors that may contribute to the ongoing burden on clearing agencies. Accordingly, the Commission preliminarily estimates the rule would impose an annual aggregate burden on each respondent of 1,128 hours, corresponding to an aggregate annual burden on all clearing agencies of 19,176 hours.[258] The Commission solicits comment regarding the accuracy of this estimate.

4. Clearing Agency Procedures To Identify and Address Conflicts of Interest

Proposed Rule 17Ad–25 would require each clearing agency to establish, implement, maintain and enforce written policies and procedures that are reasonably designed to identify and address existing or potential conflicts of interest and minimize conflicts of interest in the decision-making process of the clearing agency. As outlined above, the Commission estimates a total of 17 respondents to this requirement.[259]

The exact nature of the policies and procedures a clearing agency would establish is likely to vary between clearing agencies. For instance, legal or compliance professionals may need to work to accurately memorialize in writing the specific policy and procedure requirements regarding conflicts of interest. Information technology personnel may be relied on to develop, modify or implement computer programs that facilitate the requirements of the policies and procedures.

There are estimates of the burden imposed by similar policies and procedures requirements in Regulation NMS and in proposed requirements for security-based swap data repositories.[260] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that for PRA purposes there is similarity in the burden to create policies and procedures.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily estimates that proposed Rule 17Ad–25 would impose a one-time burden on each respondent clearing agency of 420 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 7,140 hours.[261] Also based on the estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that a burden of $40,000 in initial outside legal costs would be incurred per respondent clearing agency for an aggregate outside cost burden of $680,000 for all clearing agencies.[262] The Commission solicits comment regarding the accuracy of these estimates.

For a clearing agency to monitor, enforce, and potentially adjust its policies and procedures in connection with proposed Rule 17Ad–25, the Commission preliminarily believes these activities would impose an ongoing aggregate annual burden on each respondent clearing agency of 120 hours, corresponding to an aggregate annual ongoing burden for all respondents of 2,040 hours.[263] The Commission solicits comment regarding the accuracy of these estimates.

[256] This figure was calculated as follows: ((Chief Compliance Officer at 210 hours) + (Computer Operations Department Manager at 180 hours) + (Senior Programmer at 180 hours) + (Senior Risk Management Specialist at 40 hours)) = 610 hours × 17 respondent clearing agencies = 10,370 hours.

[257] This figure was calculated as follows: $10,000 dollars in software costs per respondent clearing agency × 17 respondent clearing agencies = $170,000.

[258] This figure was calculated as follows ((Compliance Attorney at 4 hours per business day × 260 business days per year) = 1040 hours per year + (Computer Operations Department Manager at 40 hours per year) + (Senior Programmer at 40 hours per year) + (Senior Risk Management Specialist at 8 hours per year)) = 1,128 hours per year × 17 respondent clearing agencies = 19,176 hours per year.

[259] *See supra* notes 145–148 and accompanying text.

[260] *See supra* note 157.

[261] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours to create one policy and procedure × 2 policies and procedures x 17 respondent clearing agencies = 7,140 hours. *See supra* note 195.

[262] This estimated $680,000 figure has been calculated as follows: $400 per hour cost for outside legal services × 50 hours × 2 policies and procedures × 17 clearing agencies. This is the same estimate used by the Commission for these services in the proposed consolidated audit trail rule. *See* Exchange Act Release No. 62174 (May 26, 2010), 75 FR 32556 (June 8, 2010).

[263] This figure was calculated as follows: Compliance Attorney at 60 hours × 17 respondent clearing agencies = 1,020 hours to administer one policy and procedure × 2 policies and procedures = 2,040 hours. *See supra* note 196.

5. Standards for Board or Board Committee Directors

Proposed Rule 17Ad–26 outlines the proposed governance standards that clearing agencies would be required to establish for board or board committee directors. As outlined above, the Commission estimates a total of 17 respondents to this requirement.[264]

The exact nature of the policies and procedures a clearing agency would establish is likely to vary between clearing agencies. For instance, legal or compliance professionals may need to work with a law firm to accurately memorialize in writing the specific policy and procedure requirements regarding the selection of directors. However, as noted above in the discussion of the burdens associated with proposed Rule 17Ad–25, there are estimates of similar burdens imposed by policies and procedures requirements in Regulation NMS and in the proposed requirements for security-based swap data repositories.[265] While the requirements underlying those estimates are not identical to this requirement for clearing agencies, the Commission preliminarily believes that there is sufficient similarity between them for PRA purposes that the burden would be roughly equivalent.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories, the Commission preliminarily believes that this rule would impose an aggregate one-time burden on each respondent clearing agency of 210 hours to create the minimum standards required by the rule, corresponding to a one-time aggregate burden for all clearing agencies of 3,570 hours.[266] The Commission solicits comment regarding the accuracy of this estimate.

The Commission also estimates, based on similar requirements and the corresponding burdens in Regulation NMS and for security-based swap data repositories that a total burden of $20,000 in outside legal costs would be incurred by each respondent clearing agency, corresponding to an aggregate cost burden of $340,000 for all respondent clearing agencies.[267] The Commission solicits comment regarding the accuracy of this information.

Clearing agencies would be required to administer their governance standards required by proposed Rule 17Ad–26 on an ongoing basis. The Commission expects that the exact burden of administering the governance standards would vary depending on factors that include, but are not limited to, how frequently a clearing agency elects new board members and how many board and board committee members are involved with the governance of each clearing agency. These factors would influence the time spent evaluating potential new board members as well as the time needed to assess existing board members at least annually for compliance with the standards.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS and for security-based swap data repositories, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 1,020 hours.[268] The Commission solicits comment regarding the accuracy of this information. The proposed rule also encourages clearing agencies to use a third party to facilitate completion of the board's annual assessment of its members against its governance standards. The Commission estimates that using a third party would impose an average annual burden of 20 hours on each respondent clearing agency, corresponding to aggregate of 340 hours all clearing agencies.[269] The Commission solicits comment regarding the accuracy of this estimate.

6. Designation of Chief Compliance Officer

Under proposed Rule 3Cj–1(b), a registered clearing agency's CCO would be responsible for, among other matters, (1) establishing policies and procedures for the remediation of non-compliance issues identified by the CCO and (2) establishing and following appropriate procedures for the handling of management response, remediation, retesting and closing of non-compliance issues. As outlined above, the Commission estimates a total of 17 respondents to this requirement.[270]

The exact nature of the policies and procedures a clearing agency would establish is likely to vary between clearing agencies. However, as noted in the discussion of the estimated burdens for proposed Rules 17Ad–25 and 17Ad–26, there are similarly positioned requirements and corresponding burden estimates in Regulation NMS and in the proposed requirements for security-based swap data repositories.[271] The proposed rule requirements that create the estimated PRA burden for the CCO of a security-based swap data repository[272] are highly-similar to the proposed requirements for the CCO of a clearing agency in Rule 3Cj–1(b).[273] This is because both rules are predicated on statutory provisions of the Exchange Act that contain statutory requirements that mirror one another to a large degree.[274] Therefore, the Commission preliminarily believes that for PRA purposes the burdens would be roughly equivalent.

Consequently, the Commission preliminarily estimates that the two requirements for the CCO of a clearing agency under proposed Rule 3Cj–1 would require 420 hours to create policies and procedures, corresponding to a total burden of 7,140 hours initially.[275] The Commission also preliminarily estimates 120 hours to administer each policy and procedure per year per respondent, corresponding to 1,200 hours on average annually.[276]

[264] *See supra* notes 149–152 and accompanying text.

[265] *See supra* note 157.

[266] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours × 17 respondent clearing agencies = 3,570 hours. *See supra* note 195.

[267] This estimated figure was calculated as follows: ($400 per hour cost for outside legal services × 50 hours) × 17 respondent clearing agencies = $170,000. *See supra* note 262.

[268] This figure was calculated as follows: Compliance Attorney at 60 hours × 17 respondent clearing agencies = 1,020 hours. *See supra* note 196.

[269] This figure was calculated as follows: Consultant at 20 hours × 17 respondent clearing agencies = 340 hours.

[270] *See supra* note 153–156 and accompanying text.

[271] *See supra* note 157.

[272] *See* Exchange Act Release No. 63347 (November 19, 2010), 75 FR 77306 (December 10, 2010) (proposed Rules 13n–11(c)(6),(7) and 13n–11(d), (h). *See generally* Public Law 111–203 § 763(a) (adding Section 3C(n)(6) to the Exchange Act).

[273] *Compare* Public Law 111–203 § 763(a) adding Section 3C(j) to the Exchange Act concerning requirements for the CCO of a clearing agency *with* Public Law 111–203 § 763(a) adding Section 3C(n)(6) concerning requirements for the CCO of an SDR.

[274] *Compare* Public Law 111–203 § 763(a) adding Section 3C(j) to the Exchange Act concerning requirements for the CCO of a clearing agency *with* Public Law 111–203 § 763(a) adding Section 3C(n)(6) concerning requirements for the CCO of an SDR.

[275] This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours to create one policy and procedure × 2 policies and procedures × 17 respondent clearing agencies = 7,140 hours. *See supra* note 195.

[276] This figure was calculated as follows: (Compliance Attorney at 60 hours x 17 respondent

Continued

The Commission preliminarily believes that this work will be conducted internally and solicits comments regarding the accuracy of this information. The Commission solicits comment regarding the accuracy of these estimates.

Also, based on the similarly positioned burdens in Regulation NMS and in the proposed requirements for the CCO of a security-based swaps data repository, the Commission preliminarily estimates that a total of $40,000 in initial outside legal costs would be incurred by each respondent clearing agency. This corresponds to an aggregate, one-time outside cost burden of $680,000 for all clearing agencies.[277] The Commission solicits comment regarding the accuracy of this estimate.

The CCO would also be required under proposed Rule 3Cj–1(c) to prepare, sign and submit (to the clearing agency's board of directors and audit committee (or equivalent bodies) and to the Commission) an annual compliance report that contains a description of (i) the compliance of the clearing agency with respect to the Federal securities laws and the rules and regulations thereunder, and (ii) each policy and procedure of the clearing agency of the compliance officer (including the code of ethics and conflict of interest policies of the registered clearing agency). Based upon the Commission's experience with similar reports, the Commission preliminarily estimates that this would require an average of 54 hours per respondent per year. Thus, the Commission preliminarily estimates an aggregate annual burden of 918 hours on all respondent clearing agencies.[278] Because the report will be submitted by the internal CCO, the Commission preliminarily does not expect any external costs. The Commission solicits comments regarding the accuracy of this estimate.

*E. Collection of Information Is Mandatory*

1. Standards for Clearing Agencies

a. Measurement and Management of Credit Exposures

The collection of information relating to measuring credit exposures to its participants at least once a day and limiting its exposures to potential losses from defaults by its participants in normal market conditions so that the operations of the clearing agency would not be disrupted and non-defaulting participants would not be exposed to losses that they cannot anticipate or control under proposed Rule 17Ad–22(b)(1) would be mandatory for all clearing agencies that provide CCP services.

b. Margin Requirements

The collection of information relating to using margin requirements to limit credit exposures to participants in normal market conditions and using risk-based models and parameters to set margin requirements and review them at least monthly under proposed Rule 17Ad–22(b)(2) would be mandatory for all clearing agencies that provide CCP services.

c. Financial Resources

The collection of information relating to maintaining sufficient financial resources to withstand, at a minimum, a default by the participant to which it has the largest exposure in extreme but plausible market conditions, and if the clearing agency provides CCP services for security-based swaps then a default by the two participants to which it has the largest exposures in extreme but plausible market conditions; provided that if a participant controls another participant or is under common control with another participant, then the affiliated participants shall be collectively deemed to be a single participant under proposed Rule 17Ad–22(b)(3) would be mandatory for all clearing agencies that provide CCP services.

d. Model Validation

The collection of information relating to providing for an annual model validation consisting of evaluating the performance of the clearing agency's margin models and the related parameters and assumptions associated with such models by a qualified person who does not perform functions associated with the clearing agency's margin models (except as part of the annual model validation) and does not report to a person who performs these functions under proposed Rule 17Ad–22(b)(4) would be mandatory for all clearing agencies that provide CCP services.

e. Non-Dealer Access

The collection of information relating to providing the opportunity for a person that does not perform any dealer or security-based swap dealer services to obtain membership at the clearing agency to clear securities for itself or on behalf of other persons under proposed Rule 17Ad–22(b)(5) would be mandatory for all clearing agencies that provide CCP services.

f. Net Capital Requirements

The collection of information relating to providing the opportunity for a person that maintains net capital equal to or greater than $50 million with the ability to obtain membership at the clearing agency, with any net capital requirements being scalable so that they are proportional to the risks posed by the participant's activities to the clearing agency; provided, however, that the clearing agency may provide for a higher net capital requirement as a condition for membership at the clearing agency if the clearing agency demonstrates to the Commission that such a requirement is necessary to mitigate risks that could not otherwise be effectively managed by other measures and the Commission approves the higher net capital requirement as part of a rule filing or clearing agency registration application under proposed Rule 17Ad–22(b)(7) would be mandatory for all clearing agencies that provide CCP services.

g. Record of Financial Resources

The collection of information each fiscal quarter, or at any time upon request by the Commission, relating to the calculation and maintenance of a record of the financial resources necessary to meet the requirements of proposed Rule 17Ad–22(b)(3) under proposed Rule 17Ad–22(c)(1) would be mandatory for all clearing agencies that perform CCP services.

h. Annual Audited Financial Report

The collection of information relating to the annual audited financial report that shall (i) be a complete set of financial statements of the clearing agency for the most recent two fiscal years and be prepared in accordance with U.S. GAAP, except that for a clearing agency that is a corporation or other organization incorporated or organized under the laws of any foreign country the financial statements may be prepared according to U.S. GAAP or IFRS; (ii) be audited in accordance with standards of the Public Company Accounting Oversight Board by a registered public accounting firm that is qualified and independent in accordance with Rule 2–01 of Regulation S–X (17 CFR 210.2–01); and (iii) include a report of the registered public accounting firm that complies with paragraphs (a) through (d) of Rule

clearing agencies) = 1,020 hours to administer one policy and procedure x 2 policies and procedures = 2,040 hours. *See supra* note 196.

[277] This figure was calculated as follows: (($400 per hour cost for outside legal services × 50 hours) × (2 policies and procedures)) × 17 clearing agencies = $680,000. *See supra* note 262.

[278] This figure is based on the following: ((Compliance Attorney at 50 hours) + (Senior Systems Analyst at 4 hours)) × 17 clearing agencies = 918 hours.

2–02 of Regulation S–X (17 CFR 210.2–02) under proposed Rule 17Ad–22(c)(2) would be mandatory for all clearing agencies.

i. Transparent and Enforceable Rules and Procedures

The collection of information relating to policies and procedures providing for a well founded, transparent, and enforceable legal framework for each aspect of its activities in all relevant jurisdictions under proposed Rule 17Ad–22(d)(1) would be mandatory for all clearing agencies.

j. Participation Requirements

The collection of information relating to requiring participants to have sufficient financial resources and robust operational capacity to meet obligations arising from participation in the clearing agency; have procedures in place to monitor that participation requirements are met on an ongoing basis; and have participation requirements that are objective, publicly disclosed, and permit fair and open access under proposed Rule 17Ad–22(d)(2) would be mandatory for all clearing agencies.

k. Identification and Mitigation of Custody of Assets and Investment Risk

The collection of information relating to holding assets in a manner whereby risk of loss or of delay in its access to them is minimized; and investing assets in instruments with minimal credit, market and liquidity risks under proposed Rule 17Ad–22(d)(3) would be mandatory for all clearing agencies.

l. Identification and Mitigation of Operational Risk

The collection of information relating to identifying sources of operational risk and minimizing them through the development of appropriate systems, controls, and procedures; implementing systems that are reliable, resilient and secure, and have adequate, scalable capacity; and having business continuity plans that allow for timely recovery of operations and fulfillment of a clearing agency's obligations under proposed Rule 17Ad–22(d)(4) would be mandatory for all clearing agencies.

m. Money Settlement Risks

The collection of information relating to employing money settlement arrangements that eliminate or strictly limit the clearing agency's settlement bank risks, that is, its credit and liquidity risks from the use of banks to effect money settlements with its participants; and requiring funds transfers to the clearing agency to be final when effected under proposed Rule 17Ad–22(d)(5) would be mandatory for all clearing agencies.

n. Cost-Effectiveness

The collection of information relating to being cost-effective in meeting the requirements of participants while maintaining safe and secure operations under proposed Rule 17Ad–22(d)(6) would be mandatory for all clearing agencies.

o. Links

The collection of information relating to evaluating the potential sources of risk for any link arrangements the clearing agency establishes and prudently managing those risks under proposed Rule 17Ad–22(d)(7) would be mandatory for all clearing agencies.

p. Governance

The collection of information relating to having governance arrangements that are clear and transparent to fulfill the public interest requirements in Section 17A of the Exchange Act applicable to clearing agencies, to support the objectives of owners and participants, and to promote the effectiveness of the clearing agency's risk management procedures under proposed Rule 17Ad–22(d)(8) would be mandatory for all clearing agencies.

q. Information on Services

The collection of information relating to providing market participants with sufficient information for them to identify and evaluate the risks and costs associated with using its services under proposed Rule 17Ad–22(d)(9) would be mandatory for all clearing agencies.

r. Immobilization and Dematerialization of Stock Certificates

The collection of information relating to immobilization and dematerialization of securities certificates and transferring them by book entry to the greatest extent possible under proposed Rule 17Ad–22(d)(10) would be mandatory for all clearing agencies that perform central securities depository services.

s. Default Procedures

The collection of information relating to making key aspects of the clearing agency's default procedures publicly available and establishing default procedures that ensure that the clearing agency can take timely action to contain losses and liquidity pressures and to continue meeting its obligations in the event of a participant default under proposed Rule 17Ad–22(d)(11) would be mandatory for all clearing agencies.

t. Risk Controls To Address Participants' Failure To Settle

The collection of information relating to instituting risk controls including collateral requirements and limits to cover the clearing agency's credit exposure to each participant exposure fully, and that ensure timely settlement in the event that the participant with the largest payment obligation is unable to settle when the clearing agency provides central securities depository services and extends intraday credit to participants, provided that if a participant controls another participant or is under common control with another participant then the affiliated participants shall be collectively deemed to be a single participant, under proposed Rule 17Ad–22(d)(14) would be mandatory for all clearing agencies.

u. Identification and Management of Physical Delivery Risks

The collection of information relating to stating to participants the clearing agency's obligations with respect to physical deliveries and identifying and managing the risks from those obligations under proposed Rule 17Ad–22(d)(15) would be mandatory for all clearing agencies.

2. Dissemination of Pricing and Valuation Information by Security-Based Swap Clearing Agencies That Perform Central Counterparty Services

The collection of information relating to the dissemination of pricing and valuation information of security-based swaps under proposed Rule 17Aj–1 would be mandatory for all security-based swap clearing agencies that perform CCP services.

3. Clearing Agency Policies and Procedures To Protect the Confidentiality of Trading Information of Clearing Agency Participants

The collection of information relating to the establishment, maintenance and enforcement of written policies and procedures under proposed Rule 17Ad–23 pertaining to the confidentiality of trading information would be mandatory for all clearing agencies.

4. Clearing Agency Procedures To Identify and Address Conflicts of Interest

The collection of information relating to the establishment, implementation, maintenance and enforcement of written policies and procedures reasonably designed to identify and address conflicts of interest under proposed Rule 17Ad–25 would be mandatory for all clearing agencies.

5. Standards for Board or Board Committee Directors

The collection of information relating to board or board committee directors governance standards under proposed Rule 17Ad–26 would be mandatory for all clearing agencies.

6. Designation of Chief Compliance Officer

The collection of information relating to the CCO under proposed Rule 3Cj–1 requirements would be mandatory for all clearing agencies.

*F. Confidentiality*

1. Standards for Clearing Agencies

a. Measurement and Management of Credit Exposures

The collection of information relating to the measurement and management of credit exposures under proposed Rule 17Ad–22(b)(1) would be provided to the Commission staff but not subject to public availability.

b. Margin Requirements

The collection of information relating to margin requirements under proposed Rule 17Ad–22(b)(2) would be provided to the Commission staff but not subject to public availability.

c. Financial Resources

The collection of information relating to financial resources under proposed Rule 17Ad–22(b)(3) would be provided to the Commission staff but not subject to public availability.

d. Model Validation

The collection of information relating to conducting an annual model validation under proposed Rule 17Ad–22(b)(4) would be provided to the Commission staff but not subject to public availability.

e. Non-Dealer Access

The collection of information relating to non-dealer access under proposed Rule 17Ad–22(b)(5) would be provided to the Commission staff but not subject to public availability.

f. Net Capital Requirements

The collection of information relating to the procedures for net capital requirements under proposed Rule 17Ad–22(b)(7) would be provided to the Commission staff but not subject to public availability.

g. Record of Financial Resources

The collection of information relating to the calculation and maintenance by a clearing agency that provides CCP services of a quarterly report describing the financial resources necessary to meet the requirements of proposed Rule 17Ad–22(b)(3) would be provided to the Commission staff under proposed Rule 17Ad–22(c)(1) but would not be subject to public availability.

h. Annual Audited Financial Report

The collection of information relating to the annual audited financial report published to the clearing agency's Web site under proposed Rule 17Ad–22(c)(2) would be subject to public availability.

i. Transparent and Enforceable Rules and Procedures

The collection of information relating to a clearing agency's well founded, transparent and enforceable legal framework under proposed Rule 17Ad–22(d)(1) would be provided to the Commission staff but not subject to public availability.

j. Participation Requirements

The collection of information relating to the procedures for monitoring and publicly disseminating the participation requirements under proposed Rule 17Ad–22(d)(2) would be provided to the Commission staff and would be subject to public availability.

k. Custody of Assets and Investment Risk

The collection of information relating minimizing custody and investment risk under proposed Rule 17Ad–22(d)(3) would be provided to the Commission staff but not subject to public availability.

l. Identification and Mitigation of Operational Risk

The collection of information relating to identifying and minimizing operational risk under proposed Rule 17Ad–22(d)(4) would be provided to the Commission staff but not subject to public availability.

m. Money Settlement Risks

The collection of information relating to the procedures for money settlement arrangements under proposed Rule 17Ad–22(d)(5) would be provided to the Commission staff but not subject to public availability.

n. Cost-Effectiveness

The collection of information relating to being cost-effective under proposed Rule 17Ad–22(d)(6) would be provided to the Commission staff but not subject to public availability.

o. Links

The collection of information relating to evaluating potential sources of risk in links arrangements under proposed Rule 17Ad–22(d)(7) would be provided to the Commission staff but not subject to public availability.

p. Governance

The collection of information relating to a clearing agency's governance arrangements under proposed Rule 17Ad–22(d)(8) would be provided to the Commission staff but not subject to public availability.

q. Information on Services

The collection of information relating to the provision of sufficient information to market participants under proposed Rule 17Ad–22(d)(9) would be provided to the Commission staff and market participants but not subject to public availability.

r. Immobilization and Dematerialization of Stock Certificates

The collection of information relating to the procedures for immobilizing and dematerializing stock certificates under proposed Rule 17Ad–22(d)(10) would be provided to the Commission staff but not subject to public availability.

s. Default Procedures

The collection of information relating to the establishment and maintenance of default procedures under proposed Rule 17Ad–22(d)(11) would be subject to public availability.

t. Risk Controls To Address Participants' Failure To Settle

The collection of information relating to risk controls to address participants' failure to settle under proposed Rule 17Ad–22(d)(14) would be provided to the Commission staff, but not subject to public availability.

u. Identification and Management of Physical Delivery Risks

The collection of information relating to the statement and management of physical delivery risk under proposed Rule 17Ad–22(d)(15) would be provided to the Commission staff, but not subject to public availability.

2. Dissemination of Pricing and Valuation Information by Security-Based Swap Clearing Agencies That Perform Central Counterparty Services

The collection of information relating to the dissemination of pricing and valuation information under proposed Rule 17Aj–1 would be subject to public availability.

3. Clearing Agency Policies and Procedures To Protect the Confidentiality of Trading Information of Clearing Agency Participants

The collection of information pertaining to the establishment, maintenance and enforcement of written policies and procedures pertaining to the confidentiality of trading information under proposed Rule 17Ad–23 would be provided to the Commission staff and would be subject to public availability.

4. Clearing Agency Procedures To Identify and Address Conflicts of Interest

The collection of information relating to the establishment, implementation, maintenance and enforcement of written policies and procedures reasonably designed to identify and address conflicts of interest under proposed Rule 17Ad–25 would be provided to the Commission staff and would be subject to public availability.

5. Standards for Board or Board Committee Directors

The collection of information relating to board or board committee directors governance standards under proposed Rue 17Ad–26 would be provided to the Commission staff and would be subject to public availability.

6. Designation of Chief Compliance Officer

The collection of information relating to the CCO under proposed Rule 3Cj–1 would be provided to the Commission staff and would be subject to public availability.

*G. Retention Period of Recordkeeping Requirements*

Registered clearing agencies will be required to retain all correspondence and other communications reduced to writing (including comment letters) to and from such clearing agency for a period of not less than five years, the first two years of which are to be in a place immediately available to the Commission staff for inspection and examination, pursuant to the recordkeeping requirements set forth in Rule 17a–1 of the Exchange Act.

*H. Request for Comment*

The Commission invites comments on all of the above estimates. Pursuant to 44 U.S.C. 3506(c)(2)(B), the Commission requests comment in order to: (a) Evaluate whether the collection of information is necessary for the proper performance of our functions, including whether the information will have practical utility; (b) evaluate the accuracy of our estimate of the burden of the collection of information; (c) determine whether there are ways to enhance the quality, utility and clarity of the information to be collected; and (d) evaluate whether there are ways to minimize the burden of the collection of information on those who respond, including through the use of automated collection techniques or other forms of information technology.

Persons submitting comments on the collection of information requirements should direct them to the Office of Management and Budget, Attention: Desk Officer for the Securities and Exchange Commission, Office of Information and Regulatory Affairs, Washington, DC 20503, and should also send a copy of their comments to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE., Washington, DC 20549–1090, with reference to File No. S7–8–11. Requests for materials submitted to OMB by the Commission with regard to this collection of information should be in writing, with reference to File No. S7–8–11, and be submitted to the Securities and Exchange Commission, Office of Investor Education and Advocacy, 100 F Street, NE., Washington, DC 20549–0213. As OMB is required to make a decision concerning the collections of information between 30 and 60 days after publication, a comment to OMB is best assured of having its full effect if OMB receives it within 30 days of publication.

## VI. Consideration of Costs and Benefits [279]

The Commission is proposing several new rules that would set standards for the operation and governance of clearing agencies. In part, the Dodd-Frank Act is intended to promote financial stability in the financial system of the United States by improving accountability and transparency.[280] Key aspects of the framework of the Dodd-Frank Act specifically give the Commission authority to regulate security-based swaps [281] and to prescribe regulations containing risk management standards for designated clearing entities that the Commission regulates. In addition to considering these specific concerns in formulating the proposed rules, the Commission believes that designing several of the proposed rules to be applicable to all clearing agencies promotes financial stability by facilitating prompt and accurate clearance and settlement of securities transactions consistent with Section 17A of the Exchange Act while concurrently promoting the Dodd-Frank Act's stated aims of accountability and transparency.

Proposed Rules 17Ad–22 through 17Ad–26 and 3Cj–1 would establish operational standards for registered clearing agencies and require those clearing agencies to adopt written policies and procedures pertaining to, among other matters, the confidential treatment of trading information received by the clearing agency, identifying and addressing conflicts of interest, establishing board governance standards and designating a CCO for the clearing agency. Proposed Rule 17Aj–1 would require the public dissemination of certain pricing and valuation information by clearing agencies that perform CCP services with respect to security-based swaps. Finally, the proposed amendments to existing Rule 17Ab2–1 would modify the temporary registration process for clearing agencies.

The Commission is sensitive to the costs and benefits imposed by its rules and has identified the following costs and benefits. In particular, the discussion below is focused on the costs and benefits flowing from the decisions proposed by the Commission to fulfill the mandates of the Dodd-Frank Act rather than the mandates of the Dodd-Frank Act itself. However, to the extent that the Commission's discretion is aligned to take full advantage of the benefits intended by the Dodd-Frank Act, the two types of benefits are not entirely separable. The Commission requests that commenters provide data and any other information or statistics on which they relied on to reach any conclusions.

*A. Standards for Clearing Agencies*

The standards set forth under proposed Rule 17Ad–22 build off of the recommendations of the CPSS–IOSCO RSSS and RCCP, adjusted to conform to the U.S. system for clearing agency regulation and to adopt those tailored standards as rule requirements. Included in this proposed rule is the requirement that each fiscal quarter (based on calculations made as of the last business day of the clearing agency's fiscal quarter), or at any time upon Commission request, a clearing

[279] The hourly rates use for professionals used throughout this Section VI. Consideration of Costs and Benefits are taken from the Securities Industry and Financial Markets Association's *Management & Professional Earnings in the Securities Industry 2010,* modified by the Commission's staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

[280] *See supra* note 2.

[281] *See supra* note 3.

agency that performs central counterparty services shall calculate and maintain a record of the financial resources necessary to comply with proposed Rule 17Ad–22(b)(3), as well as sufficient documentation to explain the methodology it uses to compute such financial resource requirement.

1. Benefits

The proposed standards are intended to provide benefits to clearing agencies and the markets they serve by promoting implementation of measures that would enhance the safety and efficiency of clearing agencies and reduce systemic risk. Safe and reliable clearing agencies are essential not only for the stability of the securities markets they serve but often also to payment systems, which may be used by a clearing agency or may themselves use a clearing agency to transfer collateral. The safety of securities settlement arrangements and post-trade custody arrangements is also critical to the goal of protecting the assets of investors from claims by creditors of intermediaries and other entities that perform various functions in the operation of the clearing agency.

Permitting persons who do not provide dealer or security-based swap dealer services to become members of a clearing agency, as required under proposed Rule 17Ad–22(b)(5), should foster the development of correspondent clearing arrangements that would allow dealers and security-based swap dealers, who may otherwise not be able to meet reasonable participation standards of a clearing agency, to obtain access to the clearing agency through correspondent clearing arrangements, thereby increasing competition among clearing agencies. The net capital requirements contained in proposed Rule 17Ad–22(b)(7) would help remove an overly burdensome barrier to clearing agency access for market participants with a net capital level of at least $50 million, and promote greater direct access to clearing agencies. Entities that become participants will also benefit from an elimination of fee costs that the entities might otherwise have incurred to gain indirect access to the clearing agency through existing participants with higher levels of net capital. Proposed Rule 17Ad–22(b)(7) also may facilitate greater competition among market participants of varying sizes because smaller market participants may not incur additional cost to clear and settle transactions.

Finally, the standards in proposed Rule 17Ad–22(d) have the potential to mitigate various risks associated with providing clearing agency services by establishing standards to address (1) transparent and enforceable rules and procedures; (2) participation requirements; (3) custody of assets and investment risk; (4) operational risk; (5) money settlement risk; (6) cost-effectiveness; (7) links; (8) governance; (9) information on services; (10) immobilization and dematerialization of stock certificates; (11) default procedures; (12) timing of settlement finality; (13) delivery versus payment; (14) risk controls to address participants' failures to settle; and (15) physical delivery risks. This should help to create a framework for the operation of clearing agencies that would promote sound and efficient practices by the clearing agency. Moreover, standards relating to measurement and management of credit exposures, margin requirements, and financial resources should act as a helpful tool to manage systemic risk as increasing amounts of clearance and settlement activity is centralized within clearing agencies. At the same time, requiring annual evaluations of the performance of the clearing agency's margin models should help to ensure that clearing agencies' margin models perform in a manner that facilitates prompt and accurate clearance and settlement of transactions.

2. Costs

As noted above, the standards contained in proposed Rules 17Ad–22(b)(1), (2), (3), (4), (5), (6), (7), (c)(1), (2), (d)(1), (2), (3), (4), (5), (6), (7), (8), (9), (10), (11), (12), (13), (14) and (15) would impose certain burdens and related costs on respondent clearing agencies. As discussed in section V.D.1., based on policies and procedures requirements for Regulation NMS and security-based swap data repositories and based on staff conversations with industry representatives, the Commission has estimated the burdens and related costs of these requirements for clearing agencies.

The proposed clearing agency standards in proposed Rules 17Ad–22(b)(1), (2), (3), (4), (5), (6), (7), (c)(1), (2), (d)(1), (2), (3), (4), (5), (6), (7), (8), (9), (10), (11), (12), (13), (14) and (15) would require respondent clearing agencies to create policies and procedures. The requirements would impose one-time costs of approximately $26,084,488 in the aggregate for all respondent clearing agencies.[282] The standards contained in proposed Rules 17Ad–22(b)(4), (c)(2), (d)(2), (8), (9), (11) and (15) would also impose one-time costs on clearing agencies that are related to the adjustment of systems. With respect to proposed Rules 17Ad–22(b)(2), (d)(2), (8), (9), (11) and (15), this adjustment would be related to facilitating compliance with requirements to provide information or make information available. Proposed Rule 17Ad–22(b)(4) would require one-time systems adjustments related to the capability to perform an annual model validation. These adjustments would amount to a one-time cost of approximately $4,182,480 in the aggregate for all respondent clearing agencies.[283] Consequently, this results in a total one-time burden imposed by proposed Rule 17Ad–22 of approximately $30,266,968 in the aggregate for all respondent clearing agencies.[284]

The standards contained in Rule 17Ad–22 would also impose ongoing costs on clearing agencies. For example, the proposed clearing agency standards in proposed Rules 17Ad–22(b)(1), (2), (3), (4), (5), (6), (7), (c)(1), (2), (d)(1), (2), (3), (4), (5), (6), (7), (8), (9), (10), (11), (14) and (15) would collectively require respondent clearing agencies to perform certain ongoing monitoring and enforcement activities with respect to the policies and procedures the clearing agency creates in response to the proposed standard. Accordingly, the Commission preliminarily believes that those ongoing activities would impose total annual costs of approximately $6,660,800 in the aggregate for all respondent clearing agencies.[285]

[282] This figure was calculated as follows: ((Assistant General Counsel for 87 hours at $430 per hour) + (Compliance Attorney for 77 hours at $320 per hour) + (Computer Operations Department Manager for 23 hours at $367 per hour) + (Senior Business Analyst for 23 hours at $232 per hour)) = $75,827 × 16 standards pursuant to proposed Rules 17Ad–22(d)(1), (2), (3), (4), (5), (6), (7), (8), (9), (10), (11), (14), (15) and (c)(2) = $1,213,232 × 17 respondent clearing agencies = $20,624,944) + (($75,827 × 8 standards pursuant to proposed Rules 17Ad–22(b)(1), (2), (3), (4), (5), (6), (7) and (c)(1) = $606,616 × 9 clearing agencies = $5,459,544) = $26,084,488. *See supra* note 195.

[283] This figure was calculated as follows: ((Chief Compliance Officer for 40 hours at $423 per hour) + (Computer Department Operations Manager for 40 hours at $367 per hour) + (Senior Programmer for 20 hours at $304 per hour) = $37,680 × proposed Rules 17Ad–22(d)(2), (8), (9), (11), (15) and (d)(2)) = $226,080 × 17 respondent clearing agencies = $3,843,360 + ($37,680 × 9 clearing agencies for proposed Rules 17Ad–22(b)(4) = $339,120) = $4,182,480. *See supra* note 253.

[284] This $30,266,968 figure is the sum of the one-time costs calculated in note 282, $26,084,488, plus the one-time costs calculated in note 283, $4,182,480.

[285] This figure was calculated as follows: ((Compliance Attorney for 60 hours at $320 per hour = $19,200 × 16 standards pursuant to proposed Rules 17Ad–22(d)(1), (2), (3), (4), (5), (6), (7), (8), (9), (10), (11), (12), (13), (14), (15) and (c)(2) = $307,200 × 17 respondent clearing agencies = $5,222,400) + ($19,200 × 8 standards pursuant to proposed Rules 17Ad–22(b)(1), (2), (3), (4), (5), (6), (7) and (c)(1) =

Proposed Rule 17Ad–22(b)(4) would entail ongoing costs. To meet the requirements of the proposed Rule 17Ad–22(b)(4) to provide for an annual model validation, the Commission preliminarily believes clearing agencies would hire a consulting firm that dedicates two consultants to the project. The Commission estimates that this requirement would impose an ongoing annual cost of approximately $432,000 for each respondent, which corresponds to a total annual cost of approximately $7,776,000 in the aggregate for all respondent clearing agencies.[286]

Proposed Rule 17Ad–22(b)(6) would impose ongoing costs on the nine estimated clearing agencies that provide CCP services. The rule would impose these ongoing costs to the extent that staff from the legal, compliance, risk or other departments at the clearing agency providing CCP services would be responsible for ensuring that the clearing agency's membership standards do not require participants to maintain a portfolio of a minimum size or to maintain a minimum transaction volume threshold. This gate-keeping responsibility required in Rule 17Ad–22(b)(6) is unlikely to require the complete work hours of a full-time employee. Instead, as an ongoing cost related to preventing these specific types of participation standards, the cost would likely represent a fraction of total staff time and related costs. Based on the Commission's experience regulating clearing agencies that provide CCP services, it is unlikely that such a clearing agency would frequently seek to change its membership requirements in a way that would be inconsistent with proposed Rule 17Ad–22(b)(6). Therefore, the fractional cost imposed on the clearing agency by the proposed rule would likely be small compared to the clearing agency's overall cost of paying the same staff to perform their other job responsibilities.

In addition, proposed Rule 17Ad–22(b)(7) may require a clearing agency that provides CCP services to update its policies and procedures relating to its net capital requirements if it determines that the clearing agency should provide for a higher net capital requirement (*i.e.,* higher than $50 million) as a condition for membership. This work would entail the preparation of potentially one new policy annually reflecting the clearing agency's updated net capital requirements. To meet these ongoing requirements of proposed Rule 17Ad–22(b)(7), the Commission preliminarily estimates a total annual cost of $682,443 in the aggregate for all respondent clearing agencies.[287] The proposed rule's requirement that a clearing agency that provides CCP services must provide a person with net capital equal to or greater than $50 million with the ability to obtain membership at the clearing agency (with any net capital requirements being scalable so that they are proportional to the risks posed to the clearing agency by the participant's activities) would also impose costs on the operations of the clearing agency. Specifically, certain clearing agencies that provide CCP services would likely need to revise their admission criteria so that they are scalable and still provides for effective measures to limit the risks that smaller members present to the clearing agency. This would involve implementation and oversight of any measures such as heightened margin requirements, limited access to clearing services, portfolio and transaction requirements, or other risk management measures used as part of the scalable membership classes that would be designed by the clearing agency under the proposed rule.

The requirements in proposed Rules 17Ad–22(c)(1) and (2) would also impose ongoing costs on clearing agencies. Under proposed Rule 17Ad–22(c)(1), the requirement for a clearing agency that provides CCP services to calculate and maintain a record of the financial resources necessary to meet the requirements of proposed Rule 17Ad–22(b)(3), as well as sufficient documentation to explain the methodology it uses to compute such financial resource requirement, would require the efforts of clearing agency compliance and operational personnel to create the reports, properly document them and ensure the reports and supporting documentation are properly record kept. To meet these ongoing requirements of proposed Rule 17Ad–22(c)(1), the Commission preliminarily estimates a total annual cost of $37,944.[288]

Proposed Rule 17Ad–22(c)(2) would require each clearing agency to post on its Web site an annual audited financial report. Each financial report would have to: (i) be a complete set of financial statements of the clearing agency for the most recent two fiscal years and be prepared in accordance with U.S. GAAP, except that for a clearing agency that is a corporation or other organization incorporated or organized under the laws of any foreign country the financial statements may be prepared according to U.S. GAAP or IFRS as issued by the International Accounting Standards Board; (ii) be audited in accordance with standards of the Public Company Accounting Oversight Board by a registered public accounting firm that is qualified and independent in accordance with Rule 2–01 of Regulation S–X (17 CFR 210.2–01); and (iii) include a report of the registered public accounting firm that complies with paragraphs (a) through (d) of Rule 2–02 of Regulation S–X (17 CFR 210.2–02). This requirement would necessitate work hours of compliance personnel and finance personnel at the clearing agency to compile relevant data, organize and analyze that data, and then post it to the clearing agency's Web site consistent with the rule. The requirement would also require the services of a registered public accounting firm. The Commission estimates those services would cost approximately $500,000 annually. Therefore, to meet the ongoing requirements of proposed Rule 17Ad–22(c)(2) the Commission estimates a total annual cost of approximately $10,239,984 in the aggregate for all respondent clearing agencies.[289]

Consequently, this results in a total, annual burden imposed by proposed Rule 17Ad–22 of approximately $25,397,171.[290]

Recent assessments of the registered U.S. clearing agencies support the conclusion that these entities generally meet or exceed analogous standards of operation and governance to those that are contained within Rule 17Ad–22. Those findings support a view that the

$153,600 × 9 clearing agencies = $1,382,400)) = $6,660,800. *See supra* note 196.

[286] This figure was calculated as follows: 2 Consultants for 30 hours per week at $600 per hour = $36,000 per week × 12 weeks = $432,000 per clearing agency × 9 clearing agencies = $7,776,000.

[287] This figure was calculated as follows: ((Assistant General Counsel for 87 hours at $430 per hour) + (Compliance Attorney for 77 hours at $320 per hour) + (Computer Operations Department Manager for 23 hours at $367 per hour) + (Senior Business Analyst for 23 hours at $232 per hour)) = $75,827 × 1 new policy annually in response to Rule 17Ad–22(b)(7) = $75,827 × 9 respondent clearing agencies = $682,443. *See supra* note 195.

[288] This figure was calculated as follows (Compliance Attorney for 1 hour at $320 per hour) + (Computer Operations Department Manager for 2 hours at $367)) = $1,054 per quarter × 4 quarters per year = $4216 per year × 9 clearing agencies = $37,944.

[289] This figure was calculated as follows: ((Senior Accountant for 500 hours at $198 per hour) + (Senior Systems Analyst for 8 hours at $259 per hour) + (Compliance Attorney for 4 hours at $320) = $102,352 + $500,000 for independent public accounting services = $602,352 × 17 respondent clearing agencies = $10,239,984. *See supra* notes 192 and 193.

[290] This $25,397,171 figure is the sum of the aggregate annual costs estimated in note 285, $6,660,800, plus the aggregate annual cost estimated in note 286, $7,776,000, plus the aggregate cost estimated in note 287, $682,443, plus the aggregate annual cost estimated in note 288, $37,944, plus the aggregate annual cost estimated in note 289, $10,239,984.

requirements of proposed Rule 17Ad–22 would not be likely to require the clearing agencies to build new infrastructure or modify operations to continue to meet the standards.[291] The Commission's oversight of the entities clearing CDS pursuant to the CDS Clearing Exemption Orders forms the basis for a similar belief that no associated start-up costs would be imposed because those entities already represent through the CDS Clearing Exemption Orders that they meet the CPSS–IOSCO standards for central counterparties, which impose similar requirements to those contained in proposed Rule 17Ad–22.

*B. Dissemination of Pricing and Valuation Information by Security-Based Swap Clearing Agencies That Perform Central Counterparty Services*

The Commission is proposing new Rule 17Aj–1 which would require every security-based swap clearing agency that performs CCP services to make available to the public all end-of-day settlement prices and any other prices with respect to security-based swaps that it may establish to calculate mark-to-market [292] margin requirements for its participants. Proposed Rule 17Aj–1 would also require security-based swap clearing agencies that perform CCP services to make available to the public any other pricing or valuation information with respect to security-based swaps that it otherwise publishes or makes available to its participants. Under the proposed rule, this information is not required to be made available to the public free of charge. Instead, it must be provided to the public on terms that are fair, reasonable and not unreasonably discriminatory.

1. Benefits

Proposed Rule 17Aj–1 would provide a publicly available source of pricing and valuation information for pricing and valuation in the security-based swap markets. The Commission recognizes that other market mechanism created under the Dodd-Frank Act, such as security-based swap data repositories and security-based swap execution facilities, will also generate security-based swap pricing data. Under the Dodd-Frank Act, all security-based swap transactions are required to be reported to a security-based swap data repository, or, if such data repository does not exist, to the Commission.[293] Consequently, security-based swap data repositories would consolidate post-trade information about security-based swaps that the Commission preliminarily believes would be helpful for analyzing the security-based swap market as a whole and identifying its risks.[294] Similarly, security-based swap execution facilities will provide important pre-trade information about security-based swaps.

However, the Commission preliminarily believes that pricing and valuation information generated by clearing agencies would add value beyond pre- and post-trade pricing information. Rather than basing risk management of clearance and settlement on pre- or post- trade pricing that may be stale, or may be inappropriate to facilitate a clearing agency's risk management practices for other reasons, clearing agencies frequently generate their own prices for security-based swaps, either through consensus pricing or pricing models. Those prices are then used to inform the clearing agency's margin requirements for its participants and the risk management of the clearing facility.

End-of-day pricing information is pricing during the life of a security-based swap that is not otherwise available from pre- and post- trade market sources—for instance from a security-based swap execution facility or security-based swap data repository. Therefore, the Commission preliminarily believes public availability of the end-of-day pricing information, as well as any other pricing information the security-based swap clearing agency publishes or distributes with respect to security-based swaps can provide helpful transparency to market participants about the value of similar security-based swap positions they may hold. Accordingly, the Commission preliminarily believes that requiring the information to be made publicly available on terms that are fair, reasonable and not unreasonably discriminatory improves fairness, efficiency, and market competition by providing availability to data that may otherwise be difficult for some market participants to obtain.

2. Costs

The proposed rule requiring dissemination of pricing and valuation information would impose initial and ongoing costs on security-based swap clearing agencies. To establish the necessary pricing and valuation infrastructure to satisfy Rule 17Aj–1, security-based swap clearing agencies that perform CCP services would bear the cost of establishing the applicable infrastructure capabilities. The Commission notes that entities providing CCP services for security-based swaps are currently required by the CDS Clearing Exemption Orders to disseminate pricing and valuation information.

As noted above in section V.D.2., based on staff conversations with industry representatives already subject to similar requirements under the CDS Clearing Exemption Orders, the Commission preliminarily estimates that the one-time burden for a security-based swap clearing agency that performs CCP services to comply with the requirements of proposed Rule 17Aj–1 would only involve adjustments to computing systems required as part of registration. The Commission estimates that for a clearing agency to adjust its systems beyond the specifications associated with registration would impose a one-time cost of approximately $37,680 on each respondent clearing agency, corresponding to a total one-time aggregate cost imposed on all respondent clearing agencies of approximately $226,080.[295]

To meet the requirements of the proposed rule, security-based swap clearing agencies that perform CCP services would have a continuous responsibility to make the relevant pricing and valuation information available. The Commission estimates this imposes an ongoing annual aggregate burden of $22,020 for each respondent, which corresponds to an

[291] *See generally* International Monetary Fund, Publication of Financial Sector Assessment Program Documentation—Detailed Assessment of Observance of the National Securities Clearing Corporation's Observance of the CPSS–IOSCO Recommendations for Central Counterparties 4–29 (2010), *available at http://www.imf.org/external/pubs/ft/scr/2010/cr10129.pdf;* International Monetary Fund, Publication of Financial Sector Assessment Program Documentation—Detailed Assessment of Observance of the Depository Trust Company's Observance of the CPSS–IOSCO Recommendations for Securities Settlement Systems 4–40 (2010), *available at http://www.imf.org/external/pubs/ft/scr/2010/cr10128.pdf.*

[292] *See supra* note 91 (explaining the specific meaning of "mark-to-market" in the context of the margin practices of security-based swap clearing agency margin practices).

[293] *See* Public Law 111–203, §§ 763(i) and 766(a) (adding Exchange Act Sections 13(m)(1)(G) and 13A(A)(1), respectively). The Dodd-Frank Act amends the CEA to provide for a similar regulatory framework with respect to transactions in swaps regulated by the CFTC.

[294] *See* Exchange Act Release No. 63347 (November 19, 2010), 75 FR 77306 (December 10, 2010) (discussing in Section II, Role, Regulation, and Business Models of SDRs, that the enhanced transparency provided by an SDR is important to help regulators and others monitor the build-up and concentration of risk exposures in the security-based swaps market).

[295] This figure was calculated as follows: ((Chief Compliance Officer for 40 hours at $423) + (Computer Operations Department Manager for 40 hours at $367) + (Senior Programmer for 20 hours at $304)) = $37,680 dollars × 6 respondent clearing agencies = $226,080. *See supra* note 253.

ongoing aggregate annual cost of $132,120 for all respondent clearing agencies.[296]

*C. Clearing Agency Policies and Procedures To Protect the Confidentiality of Trading Information of Clearing Agency Participants*

Proposed Rule 17Ad–23 would require each registered clearing agency to establish, maintain and enforce written policies and procedures designed to protect the confidentiality of any and all transaction information that the clearing agency receives. Such transaction information may include, but is not limited to, trade data, position data, and any non-public personal information about a clearing agency member or participant or any of its members or participant's customers. The proposed rule also provides that the required policies and procedures shall include, but are not limited to, (a) limiting access to confidential trading information of clearing members to those employees of the clearing agency who are operating the system or responsible for its compliance with any other applicable laws or rules and (b) standards controlling employees and agents of the clearing agency trading for their personal benefit or the benefit of others.

1. Benefits

The proposed standards are intended to promote implementation of adequate measures taken by a clearing agency to safeguard data, which can increase market participants' confidence in the safety and reliability of a clearing agency. Trade data stored by a clearing agency should be protected from loss, leakage, unauthorized access and other processing risks. It is necessary for a clearing agency to apply information security and system integrity objectives to its own operations to protect trade data during transmission and dissemination. These protections for trade data benefit participants by helping to ensure, for instance, that participant trade data is not leaked to other market participants who may attempt to use that information to front run participant trades or misappropriate it in other ways. Protections for trade data by a clearing agency also generate the benefit to participants of promoting the confidence among participants and their customers that use of a clearing agency to clear and settle trades will not result in economic or reputational harm to the clearing agency's users. This, in turn, promotes overall marketplace confidence in the clearance and settlement system for securities transactions.

2. Costs

Proposed Rule 17Ad–23 would impose costs on a clearing agency to establish procedures to protect the confidentiality of trading information of participants. However, the entities providing CCP services for security-based swaps pursuant to the CDS Clearing Exemption Orders already maintain and enforce safeguards to protect the confidentiality of trading information of participants as part of those orders. While the Commission notes that those respondents may not need to make additional, one-time changes to meet the requirements of proposed Rule 17Ad–23, the Commission is assuming for the purpose of this cost-benefit analysis that proposed Rule 17Ad–23 would impose one-time costs on them. As discussed above in section V.D.3., based on staff discussions with industry representatives already subject to similar requirements under the CDS Clearing Exemption Orders, the Commission has estimated the burdens and related costs of these requirements for clearing agencies.

The Commission does anticipate the rule would impose one-time costs at the remaining six clearing agencies related to the coordinated research and development costs between compliance, legal, operational, and information technology staff. Protecting confidential information in compliance with the requirements of the proposed rule would likely necessitate drawing on expertise and knowledge from each of these areas. The number of employees and number of employee hours required to deliver the necessary information could vary slightly between clearing agencies given that clearing agencies may divide the skill sets of their employees differently. However, for a clearing agency to create policies and procedures protecting the confidentiality of trading information of participants, the Commission believes the rule would impose a one-time cost on each clearing agency of approximately $227,290, corresponding to an aggregate one-time cost to all respondent clearing agencies of approximately $3,863,930.[297]

The rule would also impose ongoing costs associated with storing confidential data in the form and manner prescribed by the clearing agency's policies and procedures, which would be designed to control access to that information. Such costs are likely to include monitoring and testing of the integrity of the access controls on the data and potentially updating those controls as new technology becomes available or as the clearing agency modifies the safeguarding requirements within the policies and procedures. The Commission believes these responsibilities would impose an ongoing annual cost per clearing agency of approximately $56,942, corresponding to an annual aggregate cost to all clearing agencies of approximately $7,990,544.[298]

*D. Exemption From Clearing Agency Definition*

The Commission is proposing new Rule 17Ad–24 which would exempt from the definition of clearing agency, as defined in Section 3(a)(23)(A) of the Exchange Act, certain registered security-based swap dealers and security-based swap execution facilities.

1. Benefits

The proposed rule described in this section would provide for the exclusion of certain registered security-based swap dealers and registered security-based swap execution facilities from the definition of a clearing agency. The proposed rule is intended to avoid subjecting these entities, where appropriate, to multiple registrations when doing so would impose overlapping or duplicative requirements with marginal benefits or no benefits to safeguarding securities and funds and protecting investors.

2. Costs

The Commission anticipates any costs associated with the proposed rule are likely to be minimal. Registered security-based swap dealers and registered security-based swap execution facilities that perform certain limited clearing agency functions could rely on the proposed exemption upon determining that their clearing agency

[296] This figure was calculated as follows: Computer Operations Department Manager for 60 hours at $367 dollars per hour = $22,020 × 6 security-based swap clearing agencies = $132,120. *See supra* note 254.

[297] This figure was calculated as follows ((Chief Compliance Officer for 210 hours at $423 per hour) + (Computer Operations Department Manager for 180 hours at $367 per hour) + (Senior Programmer for 180 hours at $304 per hour) + (Risk Management Specialist for 40 hours at $192 per hour) + ($10,000 software costs)) = $227,290 × 17 respondent clearing agencies = $3,863,930. *See supra* note 256.

[298] This figure was calculated as follows: Compliance Attorney at 4 hours per business day × 260 business days per year = 1,040 hours per year at $423 per hour + ((Computer Operations Department Manager for 40 hours per year at $367 per hour) + (Senior Programmer for 40 hours per year at $304 per hour) + (Senior Risk Management Specialist at 8 hours per year at $409 per hour)) = $470,032 × 17 respondent clearing agencies = $7,990,544. *See supra* note 258.

functions are within the scope of the rule.

*E. Amendment of 17Ab2–1 Registration of Clearing Agencies*

Proposed Rule 17Ab2–1 would provide for amendments to Section 17Ab2–1 of the Exchange Act and extends certain timeframes associated with the registration of clearing agencies.

1. Benefits

A modernized temporary registration process can serve as a useful tool by giving the Commission the option to examine a clearing agency after it becomes operational, but in advance of its registration being final. For example, a newly formed security-based swap clearing agency may only be able to provide materials regarding its anticipated activities when completing its CA–1 registration form. However, there may be value in examining the security-based swap clearing agency once it becomes operational. This has the benefit of informing the Commission by observations made through examinations and/or monitoring of active operations.

2. Costs

The amendments to the Rule 17Ab2–1 relate specifically to the operations of the Commission and the timing of its ability to grant temporary registrations for clearing agencies. As a result, the Commission preliminarily believes that the proposed amendments to Rule 17Ab2–1 are unlikely to impose costs to clearing agencies other than those that currently exist.

*F. Procedures To Identify and Address Conflicts of Interest*

Proposed Rule 17Ad–25 would require registered clearing agencies to establish, implement, maintain and enforce written policies reasonably designed to identify and address existing or potential conflicts of interest and minimize conflicts of interest in decision-making at the clearing agency.

1. Benefits

Requiring a clearing agency to create written policies and procedures designed to identify conflicts of interest would help a clearing agency evaluate its particular organization and activities and determine areas that might undermine the clearing agency's core business of clearing and settling securities transactions. A documented plan provides a clear set of guidelines that can focus the clearing agency's evaluation and ensure consistency in the way those evaluations are performed. Similarly, if conflicts are identified, the policies and procedures offer a standard method of approaching those conflicts to make sure they are addressed. The procedures would also provide a documented plan against which the Commission could evaluate a clearing agency's efforts to mitigate conflicts and provide the Commission with a better understanding of those areas of operation and organization about which a clearing agency may be particularly concerned.

2. Costs

Creating written policies and procedures under proposed Rule 17Ad–25 that are reasonably designed to identify and address conflicts of interest would necessitate an evaluation by each clearing agency of the areas in its operation that are likely to be susceptible to conflicts of interest. This review is an exercise likely to require collaboration between the board of directors of the clearing agency and senior management given that many of the potential conflicts are likely to revolve around the participant admissions and voting rights practices of the clearing agency. After the review, the Commission anticipates that the compliance or legal staff of the clearing agency would be assigned to draft policies and procedures.

As discussed in section V.D.4., the Commission preliminarily believes that there are analogous policies and procedures requirements for Regulation NMS and in the proposed requirements for security-based swap data repositories that are informative of the burdens and related costs to clearing agencies under proposed Rule 17Ad–25. The Commission believes that the one-time cost to research and create the policies and procedures would be approximately $191,654 for each clearing agency, corresponding to a one-time aggregate cost to all clearing agencies of approximately $3,258,118.[299] Costs would also be incurred by the clearing agency to monitor and enforce the policies and procedures. The Commission preliminarily believes this would impose an annual cost of approximately $38,400 per clearing agency, corresponding to an annual aggregate burden to all clearing agencies of approximately $652,800.[300]

*G. Standards for Board or Board Committee Directors*

Proposed Rule 17Ad–26 would set forth governance standards that clearing agencies would be required to establish with respect to their board members and board committee directors. These standards would include at least the following areas: (i) A clear articulation of the roles and responsibilities of directors serving the clearing agency's board and any board committees; (ii) director qualifications providing criteria for expertise in the securities industry, clearance and settlement of securities transactions, and financial risk management; (iii) disqualifying factors concerning serious legal misconduct, including violations of the Federal securities laws; and (iv) policies and procedures for the periodic review by the board or a board committee of the performance of its individual members.

1. Benefits

Clearing agencies are at the heart of the settlement process. Moreover, because their activities are subject to significant economies of scale, many are sole providers of clearing and settlement services to the market they serve. Therefore, their performance is a critical determinant of the safety and efficiency of those markets. No single set of governance arrangements is appropriate for all clearing agencies within the various securities markets and regulatory schemes. However, an effectively governed clearing agency should meet certain key minimum requirements. Among these are delivering sound risk management; ensuring a clear separation between reporting lines for risk management and other clearing agency operations, meeting public interest requirements, identifying those principally responsible for achieving the clearing agencies governance objectives, and disclosing the extent to which these objectives have been met.

Requiring registered clearing agencies to establish standards for their board and board committee members helps to ensure that well-qualified individuals contribute to effective governance of a clearing agency. Board members who can provide guidance by drawing on expertise in the securities industry, clearance and settlement, and risk management are well positioned to

[299] This figure was calculated as follows: ((Assistant General Counsel for 87 hours at $430 per hour) + (Compliance Attorney for 77 hours at $320 per hour) + (Computer Operations Department Manager for 23 hours at $367 per hour) + (Senior Business Analyst for 23 hours at $232 per hour)) = $75,827 × 2 policies and procedures + $40,000 in one-time outside legal costs = $191,654 × 17 respondent clearing agencies = $3,258,118. *See supra* notes 261 and 262.

[300] This figure was calculated as follows: Compliance Attorney for 60 hours at $320 per hour = $19,200 × 2 policies and procedures = $38,400 × 17 respondent clearing agencies = $652,800. *See supra* note 263.

make decisions that account for the positions of the various participants in the market the clearing agency serves as well as to balance those perspectives with the goals of stability and efficiency of the clearing agency. In the interest of promoting informed and balanced decision making in governance, requiring each clearing agency to establish governance standards that include disqualifying factors concerning serious legal misconduct, including violations of the Federal securities laws, would help clearing agencies evaluate whether persons who have been found to have violated the securities laws, or other similar laws or statutes, may not be fit to serve on the clearing agency's board or board committees.

Proposed Rule 17Ad–26 would also benefit the clearing agency and its participants by creating a degree of certainty in the role and responsibility of each director and in defining instances appropriate for removal of a director. The requirement for a clear articulation of the role and responsibility of each director focuses the governance resources of the clearing agency and provides commonly understood boundaries with respect to what is expected of each director. Clearly articulating those expectations can help the directors understand how to make individual contributions to the governance of the clearing agency as well as the ways in which they are expected to work with one another to govern the clearing agency effectively.

Finally, requiring clearing agencies to establish policies and procedures for the periodic review by the board or a board committee of the performance of its individual members would support prompt and accurate clearance and settlement because directors play a vital role in the decision-making processes of the clearing agency. These reviews would promote focused analysis on the contributions that directors make to the clearing agency and how those contributions are particularly valuable or could be adjusted or improved to better support the clearing agency's ability to operate in effectively.

2. Costs

Proposed Rule 17Ad–26 would set forth governance standards applicable to a clearing agency's board members and board committee directors. The rule would require clearing agencies to adopt procedural frameworks that inform the governance of the clearing agency.

Proposed Rule 17Ad–26 would require a clearing agency to incur research and development costs associated with creating standards for its board members and board committee members. The Commission anticipates that there would likely need to be a coordinated effort between different business units within a clearing agency to develop these standards. As discussed in section V.D.5., the Commission preliminarily believes that there are analogous policies and procedures requirements for Regulation NMS and in the proposed requirements for security-based swap data repositories that are informative of the burdens and related costs for clearing agencies under proposed Rule 17Ad–26. The Commission believes that the one-time cost to a clearing agency imposed by the rule would be approximately $95,827, corresponding to a one-time aggregate cost to all clearing agencies of approximately $1,629,059.[301]

Also involved would be the time of the clearing agency's employees that would be devoted to maintaining application of the standards to the incumbent directors, evaluating new directors and evaluating the incumbent directors on an annual basis. For example, the Commission preliminarily believes that a compliance attorney at a clearing agency may be asked to update the clearing agency's standards to clearly reflect the roles and responsibilities of the clearing agency's directors. Similarly, time of a compliance attorney may be needed to amend the standards with respect to director qualifications and disqualifying factors for service if the clearing agency decides to make changes to those aspects of its governance standards. The Commission preliminarily believes that the annual cost to each clearing agency would be approximately $19,200, corresponding to an annual aggregate cost to all clearing agencies of approximately $326,000.[302] In addition, the Commission preliminarily believes that third party facilitation of the annual review of the incumbent board members would also impose an ongoing annual cost of $6,000 for each respondent, which corresponds to a total annual cost of $102,000 in the aggregate for all respondent clearing agencies.[303] An employee at the clearing agency may be expected to help arrange and coordinate such a third-party review of the clearing agency's board members, which would also factor into the ongoing, annual cost to a clearing agency.

*H. Proposed Rule 3Cj–1 Designation of Chief Compliance Officer*

Proposed Rule 3Cj–1 would incorporate the requirements of Section 3Cj of the Exchange Act and impose additional requirements. Proposed Rule 3Cj–1 would require each registered clearing agency to designate a CCO. Under proposed Rule 3Cj–1(b), the CCO would be responsible for, among other matters, establishing policies and procedures for the remediation of non-compliance issues identified by the CCO and establishing and following appropriate procedures for the prompt handling of management response, remediation, retesting, and closing of non-compliance issues.

Under Proposed Rule 3Cj–1(c), the CCO would also be responsible for preparing and signing an annual compliance report that contains a description of (i) the compliance of the clearing agency with respect to the Federal securities laws and the rules and regulations thereunder, and (ii) each policy and procedure of the clearing agency of the compliance officer (including the code of ethics and conflict of interest policies of the registered clearing agency). This compliance report must accompany each appropriate financial report of the clearing agency that is required to be furnished to the Commission pursuant to the Exchange Act and the rules thereunder and include a certification that, under penalty of law, the compliance report is accurate and complete.

Additionally, the compliance report would be required to: (i) Be submitted to the board of directors and audit committee (or equivalent bodies) of the clearing agency promptly after the date of execution of the required certification and prior to filing of the report with the Commission; (ii) be filed with the Commission in a tagged data format in accordance with the instructions contained in the EDGAR Filer Manual, as described in Rule 301 of Regulation S–T; and (iii) be filed with the Commission within 60 days after the end of the fiscal year covered by such report.

1. Benefits

Proposed Rule 3Cj–1 is designed to ensure that clearing agencies comply with Federal securities laws, including the Exchange Act and the rules and

[301] This figure was calculated as follows: ((Assistant General Counsel for 87 hours at $430 per hour) + (Compliance Attorney for 77 hours at $320 per hour) + (Computer Operations Department Manager for 23 hours at $367 per hour) + (Senior Business Analyst for 23 hours at $232 per hour)) = $75,827 + $20,000 in one-time outside legal costs = $95,827 × 17 respondent clearing agencies = $1,629,059. *See supra* notes 266 and 267.

[302] This figure was calculated as follows: Compliance Attorney for 60 hours at $320 per hour = $19,200 × 17 respondent clearing agencies = $326,400. *See supra* note 268.

[303] This figure was calculated as follows: One Consultant for 20 hours at $600 per hour = $12,000 × 17 respondent clearing agencies = $204,000. *See supra* note 269.

regulations promulgated thereunder. Although entities currently operating as clearing agencies already may have CCOs in place, Section 3C(j) of the Exchange Act and proposed Rule 3Cj–1 would make it a required practice.

The designation of a CCO would help ensure that each clearing agency complies with the written policies and procedures it adopts. The Commission expects requiring this safeguard would in turn facilitate accurate data reporting by clearing agencies to the Commission and improve the Commission's understanding of operations across all the clearing agencies it oversees.

Proposed Rule 3Cj–1 would focus on creating a compliance structure that is transparent and minimizes conflicts. Section 3C(j) of the Exchange Act provides flexibility in permitting the CCO to report either to the clearing agency's board or to a senior officer. Because the Commission is concerned that a clearing agency's commercial interests might discourage a clearing agency's CCO from making forthright disclosure about compliance failures of the clearing agency, the proposed rule would insulate the CCO from management pressures by preventing a senior officer of a clearing agency from removing the CCO or determining the CCO's compensation without the approval of a majority of the clearing agency's board. This would provide the benefit of aligning the CCO's position within the clearing agency with having the CCO serve as a mechanism that freely encourages compliance.

The reliability of clearance and settlement services depends on the integrity of a clearing agency's operations. As a result of the proposed rule, the accuracy, reliability, and integrity of the clearing agency would be less likely to be harmed by violations of the securities laws because experience has shown that strong internal compliance programs lower the likelihood of securities laws violations and enhance the likelihood that any violations that do occur will be detected and corrected. The designation of a CCO, who will, among other things, monitor the clearing agency's compliance with the Exchange Act (including Section 17A) and the rules and regulations thereunder and with the relevant clearing agency policies and procedures, will help ensure that each clearing agency complies with the written policies and procedures it adopts.

2. Costs

As discussed in section V.D.6., the Commission preliminarily believes that there are analogous policies and procedures requirements for Regulation NMS and in the proposed requirements for security-based swap data repositories that are informative of the burdens and related costs for clearing agencies under proposed Rule 3Cj–1.

The establishment of a designated CCO and compliance with the accompanying responsibilities of a CCO would impose certain costs on each clearing agency. The Commission estimates that the average initial costs associated with establishing policies and procedures for the remediation of non-compliance issues identified by the CCO and establishing and following appropriate procedures for the handling, management response, remediation, retesting, and closing of non-compliance issues would require approximately 420 hours of employee time and approximately $40,000 for each clearing agency, and the average ongoing paperwork cost would be 120 hours for each clearing agency. In addition, each clearing agency would be required to hire a CCO to comply with the proposed rules, at an annual cost of approximately $761,400 for each clearing agency.[304] Therefore, the aggregate initial estimated dollar cost per year to each clearing agency would be approximately $191,654 for each respondent clearing agency, corresponding to an aggregate initial estimated cost to all respondent clearing agencies of approximately $3,258,118 [305] and the aggregate ongoing estimated dollar cost per year would be approximately $13,596,600 [306] to comply with the proposed rule.

The Commission estimates that the average ongoing paperwork cost associated with preparing, signing and submitting annual compliance reports pursuant to proposed Rule 3Cj–1(c)(iii) and (iv) would be 54 hours for each respondent clearing agency, corresponding to an annual cost of $17,036 for each clearing agency and an aggregate annual cost of $289,612 for all respondent clearing agencies.[307]

The Commission believes that currently-existing clearing agencies already maintain compliance programs that are overseen by a CCO or an individual who effectively serves as a CCO. In addition, such clearing agencies may prepare compliance reports presented to senior management and/or the clearing agency's board and board committees as part of their current business practice. Therefore, the Commission expects that clearing agencies with substantial commitments to compliance would probably incur only minimal costs in connection with the adoption of the proposed rule. However, for a clearing agency that does not already prepare these types of annual compliance reports as part of its compliance program, the requirements under proposed Rule 3Cj–1 would likely require the labor of clearing agency staff and impose direct costs on the clearing agency as described above.

*I. Request for Comment*

The Commission solicits comments on the benefits and costs related to proposed Rules 17Ad–22, 17Ad–23, 17Ad–24, 17Ad–25, 17Ad–26, 17Ab2–1, 3Cj–1 and 17j–1. The Commission specifically requests comments on the initial and ongoing costs associated with these rules and the costs associated with any personnel that may be necessary to support compliance with the rules. Are there additional costs that the Commission should consider? Are there alternatives that the Commission should consider? Do the estimates accurately reflect the costs that are discussed? Please describe and, to the extent practicable, quantify the costs associated with any comments that are submitted.

The Commission requests data to quantify the costs and the value of the benefits discussed above. The Commission seeks estimates of these costs and benefits, as well as any costs and benefits not addressed, which may result from the adoption of the proposed rules. Commenters should provide analysis and empirical data to support their views.

[304] This figure was calculated as follows: Chief Compliance Officer for 1,800 hours at $423 per hour = $761,400. *See supra* note 279 regarding hourly rates for professionals taken from SIFMA's *Management & Professional Earnings in the Securities Industry 2010,* and modified by the Commission's staff.

[305] This figure was calculated as follows: ((Assistant General Counsel for 87 hours at $430 per hour) + (Compliance Attorney for 77 hours at $320 per hour) + (Computer Operations Department Manager for 23 hours at $367 per hour) + (Senior Business Analyst for 23 hours at $232 per hour)) = $75,827 × 2 policies and procedures + $40,000 in one-time outside legal costs = $191,654 × 17 respondent clearing agencies = $3,258,118. *See supra* notes 275 and 277.

[306] This figure was calculated as follows: Compliance Attorney for 60 hours at $320 per hour = $19,200 × 2 policies and procedures = $38,400 + $761,400 for the annual salary of a Chief Compliance Officer = $799,800 × 17 respondent clearing agencies = $13,596,600. *See supra* notes 276 and 304.

[307] This figure was calculated as follows: ((Compliance Attorney for 50 hours at $320 per hour) + (Senior Systems Analyst for 4 hours at $259 per hour)) = $17,036 × 17 respondent clearing agencies = $289,612. *See supra* note 278.

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

Section 23(a) of the Exchange Act [308] requires the Commission, when making rules and regulations under the Exchange Act, to consider the effect a new rule would have on competition. Section 23(a)(2) prohibits the Commission from adopting any rule that would impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act.[309] Section 3(f) of the Exchange Act [310] requires the Commission, when engaging in rulemaking that requires it to consider whether an action is necessary or appropriate in the public interest, to consider, in addition to the protection of investors, whether the action would promote efficiency, competition, and capital formation.

The economic effects of the proposed rules were discussed in detail in the costs and benefits section.[311] These effects encompassed effects on economic efficiency, competition, and capital formation.

To reiterate, proposed Rules 17Ad–22 through 17Ad–26, 17Aj–1, 3Cj–1 and the proposed amendments to Rule 17Ab2–1 would set standards for the operation and governance of registered clearing agencies. These proposed rules are intended to further the purposes of the Exchange Act and to promote transparency and accountability consistent with the stated goals of the Dodd-Frank Act.[312]

Evidence from the securities markets suggests that clearing agencies over the long-run tend to converge to a small number of entities or even a single entity. In part, the Commission preliminarily believes that this is because clearing activities are characterized by high start-up costs and low marginal costs so that there are large economies of scale. For example, currently all trades executed on the eight U.S. based options exchanges are cleared at The Options Clearing Corporation, and trades executed on the U.S. equity markets, composed of exchanges, alternative trading platforms, and OTC trading, are cleared at National Securities Clearing Corporation. In this same way, it is possible that a single security-based swap clearing agency may prove itself through market forces to be the most-efficient mechanism to serve all security-based swap clearing participants by delivering the lowest-cost services.

As noted above, the current market structure for clearing agencies includes four registered clearing agencies and four entities operating pursuant to the CDS Clearing Exemption Orders that are eligible to become registered security-based swap clearing agencies pursuant to the Deemed Registered Provision of the Dodd-Frank Act. In addition, the Commission preliminarily believes there may be entities using instrumentalities of interstate commerce to perform collateral management, trade matching, Tear Up Services or similar security-based swap lifecycle event services that consequently may trigger the clearing agency registration requirement.[313]

The intent of the proposed rules concerning standards for clearing agency operations and governance standards of clearing agencies is to promote the prompt and accurate clearance and settlement of securities transactions, including security-based swap transactions, by requiring certain minimum standards at clearing agencies. The Commission preliminarily believes that these requirements would ensure resilient and cost-effective clearing agency operations as well as promote transparent and effective clearing agency governance that would consequently support confidence among market participants in clearing agencies' ability to serve as efficient mechanisms for clearance and settlement and to facilitate capital formation.

Additionally, the Commission believes that proposed Rule 17Aj–1 would support efficiency and the capital formation process by promoting security-based swap price transparency so that market participants have access to more information to value their security-based swap positions. Under the Dodd-Frank Act, all security-based swap transactions are required to be reported to a security-based swap data repository, or, if no such data repository exists, to the Commission.[314] Consequently, security-based swap data repositories consolidate post-trade information about security-based swaps. The Commission preliminarily believes this is helpful for analyzing the security-based swap market as a whole and identifying its risks.[315] Similarly, security-based swap execution facilities provide important pre-trade information about security-based swaps. In addition, there are also financial services information firms that provide certain security-based swap pricing data.

However, the Commission preliminarily believes that the pricing and valuation information generated by security-based swap clearing agencies adds value beyond these pre- and post-trade pricing sources as well as information that may be available from firms that provide financial services data. This is because proposed Rule 17Aj–1 would require a security-based swap clearing agency that performs CCP services to produce end-of-day settlement prices for all security-based swaps that it clears. This end-of-day pricing information represents pricing during the life of a security-based swap that is unique because it is not available from pre- and post-trade sources.

The Commission also preliminarily believes that this information is distinct from pricing information made available by firms that sell certain security-based swap pricing date, because each clearing agency's prices are generated daily while pricing information available through other sources may rely on various methods to derive a price—for instance an average of the bid and ask for a particular security-based swap or an executed trade price that would otherwise be stale but that has been adjusted through certain modeling practices to estimate a current price. Therefore, the Commission preliminarily believes that the public availability of these end-of-day settlement prices, as well as any other pricing information the security-based swap clearing agency publishes or distributes with respect to security-based swaps can provide helpful transparency to market participants about the current value of their security-based swap positions. Accordingly, the Commission preliminarily believes that requiring this information to be made publicly available on terms that are fair, reasonable and not unreasonably discriminatory improves fairness, efficiency, and market competition by

[308] 15 U.S.C. 78w(a).

[309] 15 U.S.C. 78w(a)(2).

[310] 15 U.S.C. 78c(f).

[311] *See* discussion *supra* at Section VI. Consideration of Costs and Benefits and accompanying subsections A. through E.

[312] *See supra* note 2 and accompanying text.

[313] *See supra* note 101 and accompanying text (noting that this list of services that may trigger clearing agency registration is not exhaustive and urging every security-based swap lifecycle event service provider to consider whether their function places them within the clearing agency definition).

[314] *See* Public Law 111–203, §§ 763(i) and 766(a) (adding Exchange Act Sections 13(m)(1)(G) and 13A(A)(1), respectively). The Dodd-Frank Act amends the CEA to provide for a similar regulatory framework with respect to transactions in swaps regulated by the CFTC.

[315] *See* Exchange Act Release No. 63347 (November 19, 2010), 75 FR 77306 (December 10, 2010) (discussing in Section II, Role, Regulation, and Business Models of SDRs, that the enhanced transparency provided by an SDR is important to help regulators and others monitor the build-up and concentration of risk exposures in the security-based swap market).

providing availability to pricing information that may otherwise be difficult for some market participants to obtain and that, among other benefits, would allow those market participants to be better-informed about the fair value of their security-based swap positions and to try to more efficiently manage the utility of those positions within their portfolio.

The Commission requests comment on the possible effects of proposed Rules 17Ad–22, 17Ad–23, 17Ad–24, 17Ad–25, 17Ad–26, 17Aj–1, 3Cj–1 and the amendments to Rule 17Ab2–1 on efficiency, competition, and capital formation. The Commission requests that commenters provide views and supporting information regarding any such effects. The Commission recognizes that such effects may be difficult to quantify. The Commission seeks comment on possible anti-competitive effects of the proposed rules not already identified. The Commission also requests comments regarding the competitive effects of pursuing alternative regulatory approaches that are consistent with Sections 763 and 805 of the Dodd-Frank Act and Section 17A of the Exchange Act. In addition, the Commission requests comment on how the other provisions of the Dodd-Frank Act for which Commission rulemaking is required will interact with and influence the competitive effects of the proposed rules under proposed Rules 17Ad–22 through 17Ad–26, 17Aj–1, 3Cj–1 and the amendments to Rule 17Ab2–1.

## VIII. Consideration of Impact on the Economy

For purposes of the Small Business Regulatory Enforcement Fairness Act of 1996 ("SBREFA"),[316], the Commission must advise the OMB as to whether the proposed rule constitutes a "major" rule. Under SBREFA, a rule is considered "major" where, if adopted, it results or is likely to result in: (i) An annual effect on the economy of $100 million or more (either in the form of an increase or a decrease); (ii) a major increase in costs or prices for consumers or individual industries; or (iii) significant adverse effect on competition, investment or innovation. If a rule is "major," its effectiveness will generally be delayed for sixty days pending Congressional review.

The Commission requests comment on the potential impact of proposed Rules 17Ad–22 through 17Ad–26, 17Aj–1, 3Cj–1 and the amendments to Rule 17Ab2–1 on the economy on an annual basis, any potential increase in costs or prices for consumers or individual industries, and any potential effect on competition, investment or innovation. Commenters are requested to provide empirical data and other factual support for their view to the extent possible.

## IX. Regulatory Flexibility Act Certification

The Regulatory Flexibility Act ("RFA")[317] requires the Commission, in promulgating rules, to consider the impact of those rules on small entities. Section 603(a)[318] of the Administrative Procedure Act,[319] as amended by the RFA, generally requires the Commission to undertake a regulatory flexibility analysis of all proposed rules to determine the impact of such rulemaking on "small entities."[320] Section 605(b) of the RFA states that this requirement shall not apply to any proposed rule which, if adopted, would not have a significant economic impact on a substantial number of small entities.[321]

### *A. Registered Clearing Agencies*

Proposed Rules 17Ad–22 through 17Ad–26, 17Aj–1, 3Cj–1 and amended Rule 17Ab2–1 would apply to all registered clearing agencies and set standards for the operation and governance of such clearing agencies. For the purposes of Commission rulemaking and as applicable to proposed Rules 17Ad–22 through 17Ad–26, 17Aj–1, 3Cj–1 and amended Rule 17Ab2–1, a small entity includes, when used with reference to a clearing agency, a clearing agency that (i) compared, cleared and settled less than $500 million in securities transactions during the preceding fiscal year, (ii) had less than $200 million of funds and securities in its custody or control at all times during the preceding fiscal year (or at any time that it has been in business, if shorter) and (iii) is not affiliated with any person (other than a natural person) that is not a small business or small organization.[322] Under the standards adopted by the Small Business Administration, small entities in the finance industry include the following: (i) For entities engaged in investment banking, securities dealing and securities brokerage activities, entities with $6.5 million or less in annual receipts; (ii) for entities engaged in trust, fiduciary and custody activities, entities with $6.5 million or less in annual receipts; and (iii) funds, trusts and other financial vehicles with $6.5 million or less in annual receipts.[323]

Based on the Commission's existing information about the clearing agencies currently registered with the Commission and the four entities clearing security-based swaps pursuant to the CDS Clearing Exemption Orders,[324] the Commission preliminarily believes that such entities exceed the thresholds defining "small entities" set out above. While other clearing agencies may emerge and become eligible to operate as clearing agencies and while other security-based swap lifecycle event service providers may be required to register as clearing agencies, the Commission preliminarily does not believe that any such entities would be "small entities" as defined in Exchange Act Rule 0–10.[325] Furthermore, we believe it is unlikely that any clearing agencies, security-based swap clearing agencies or security-based swap lifecycle event services providers would have annual receipts of less than $6.5 million. Accordingly, the Commission believes that any registered clearing agencies will exceed the thresholds for "small entities" set forth in Exchange Act Rule 0–12.

### *B. Certification*

In the Commission's preliminary view, proposed Rules 17Ad–22 through 17Ad–26, 17Aj–1, 3Cj–1 and amended Rule 17Ab2–1 would not have a significant economic impact on a substantial number of small entities for the purposes of the RFA. For the reasons described above, the Commission certifies that the proposed rules would not have a significant economic impact on a substantial number of small entities. The Commission requests comment regarding this certification. The Commission requests that commenters describe the nature of any impact on small entities, including clearing agencies, other counterparties to security-based swap transactions and

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

[317] 5 U.S.C. 601 *et seq.*

[318] 5 U.S.C. 603(a).

[319] 5 U.S.C. 551 *et seq.*

[320] Section 601(b) of the RFA permits agencies to formulate their own definitions of "small entities." The Commission has adopted definitions for the term "small entity" for the purposes of rulemaking in accordance with the RFA. These definitions, as relevant to this proposed rulemaking, are set forth in Rule 0–10, 17 CFR 240.0–10.

[321] *See* 5 U.S.C. 605(b).

[322] 17 CFR 240.0–10(d).

[323] 13 CFR 121.201, Section 52.

[324] As of July 21, 2010, the following four clearing agencies are eligible to clear security-based swaps as a result of having been granted temporary exemptive orders to operate as clearing agencies for CDS: CME, Eurex, ICE Trust and ICE Clear Europe.

[325] *See* 17 CFR 240.0–10(d). The Commission based this determination on its review of public sources of financial information about existing CCPs serving the OTC derivatives market and lifecycle event service providers.

security-based swap lifecycle event service providers, and provide empirical data to support the extent of the impact.

## X. Statutory Basis and Proposed Rule Text

Pursuant to the Exchange Act, particularly, Sections 17A(d) thereof, 15 U.S.C. 78q–1(d), Sections 17A(i), 17A(j) and 3C(j) thereof, Public Law 111–203, § 763, 124 Stat. 1841 (2010), and Sections 30(b) and 30(c) thereof, 15 U.S.C. 78dd(b) and (c), and Section 805(a)(2) of the Clearing Supervision Act, 12 U.S.C. 5464(a)(2), the Commission proposes: (1) New Rules 17Ad–22(a), 17Ad–22(d), 17Ad–23, 17Ad–24, 17Ad–25, 17Ad–26 and 3Cj–1, which would govern clearing agencies; (2) new Rules 17Ad–22(b) and (c), which would govern clearing agencies that perform central counterparty services; (3) new Rule 17Aj–1, which would govern security-based swap clearing agencies that provide central counterparty services; and (4) to amend Rule 17Ab2–1.

## List of Subjects in 17 CFR Part 240

Reporting and recordkeeping requirements, Securities.

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

## PART 240—GENERAL RULES AND REGULATIONS, SECURITIES EXCHANGE

1. The authority citation for Part 240 is amended by adding the following citations in numerical order to read as follows:

**Authority:** 15 U.S.C. 77c, 77d, 77g, 77j, 77s, 77z–2, 77z–3, 77eee, 77ggg, 77nnn, 77sss, 77ttt, 78c, 78d, 78e, 78f, 78g, 78i, 78j, 78j–1, 78k, 78k–1, 78*l,* 78m, 78n, 78o, 78o–4, 78p, 78q, 78q–1, 78s, 78u–5, 78w, 78x, 78*ll,* 78mm, 80a–20, 80a–23, 80a–29, 80a–37, 80b–3, 80b–4, 80b–11, and 7201 *et seq.;* 18 U.S.C. 1350; and 12 U.S.C. 5221(e)(3), unless otherwise noted.

* * * * *

Section 240.3Cj–1 is also issued under Pub. L. 111–203, § 763, 124 Stat. 1841 (2010).

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Sections 240.17Ad–22 through 240.17Ad–26 are also issued under 12 U.S.C. 5464(a)(2).

* * * * *

2. Section 240.3Cj–1 is added to read as follows:

### § 240.3Cj–1 Designation of chief compliance officer.

(a) *In general.* Each clearing agency shall designate a chief compliance officer. The compensation and removal of the chief compliance officer shall require the approval of a majority of the clearing agency's board.

(b) *Duties.* The chief compliance officer shall:

(1) Report directly to the board of directors or to the senior officer of the clearing agency;

(2) In consultation with its board, a body performing a function similar thereto, or the senior officer of the registered clearing agency, resolve any conflicts of interest that may arise;

(3) Be responsible for administering each policy and procedure that is required to be established pursuant to section 3C of the Act (15 U.S.C. 78c–3) and the rules and regulations thereunder;

(4) Ensure compliance with the Act and the rules and regulations thereunder;

(5) Establish policies and procedures for the prompt remediation of any non-compliance issues identified by the chief compliance officer; and

(6) Establish and follow appropriate procedures for the prompt handling, management response, remediation, retesting, and closing of non-compliance issues.

(c) *Annual Reports*—(1) *In general.* The chief compliance officer shall annually prepare and sign a report that contains a description of:

(i) The compliance of the clearing agency with respect to the Federal securities laws and the rules and regulations thereunder; and

(ii) Each policy and procedure of the clearing agency of the compliance officer (including the code of ethics and conflict of interest policies of the registered clearing agency).

(2) *Requirements.* An annual compliance report under this section shall:

(i) Accompany each appropriate financial report of the clearing agency that is required to be furnished to the Commission pursuant to the Act and the rules thereunder;

(ii) Include a certification that, under penalty of law, the compliance report is accurate and complete;

(iii) Be submitted to the board of directors and audit committee (or equivalent bodies) of the clearing agency promptly after the date of execution of the required certification and prior to filing of the report with the Commission; and

(iv) Be filed with the Commission in a tagged data format in accordance with the instructions contained in the EDGAR Filer Manual, as described in Rule 301 of Regulation S–T (17 CFR 232.301).

(v) Be filed with the Commission within 60 days after the end of the fiscal year covered by such report.

(d) For purposes of this section, references to senior officer shall include the chief executive officer, or other equivalent officer.

3. Section 240.17Ab2–1 is amended by revising paragraph (c) to read as follows:

### § 240.17Ab2–1 Registration of clearing agencies.

* * * * *

(c)(1) The Commission, upon the request of a clearing agency or upon the election of the Commission, may grant registration of the clearing agency in accordance with sections 17A(b) and 19(a)(1) of the Act for a specific period of time and may exempt, other than for purposes of section 17A(g) of the Act, the registrant from one or more of the requirements as to which the Commission is directed to make a determination pursuant to paragraphs (A) through (I) of section 17A(b)(3) of the Act, provided that any such registration shall be effective only for twenty-four months from the date the registration is made effective (or such longer period as the Commission may provide by order).

(2) In the case of any clearing agency registered in accordance with paragraph (c)(1) of this section, not later than fifteen months from the date such registration is made effective (or such longer period as the Commission may provide by order) the Commission either will grant registration in accordance with sections 17A(b) and 19(a)(1) of the Act, without, as applicable, exempting the registrant from one or more of the requirements as to which the Commission is directed to make a determination pursuant to subparagraphs (A) through (I) of section 17A(b)(3) of the Act or without limiting the duration of the registration, or will institute proceedings in accordance with section 19(a)(1)(B) of the Act to determine whether registration should be denied at the expiration of the registration granted in accordance with paragraph (c)(1) of this section.

4. Section 240.17Ad–22 is added to read as follows:

### § 240.17Ad–22 Standards for clearing agencies.

(a) *Definitions*—(1) *Central counterparty* means a clearing agency that interposes itself between the counterparties to securities transactions, acting functionally as the buyer to every seller and the seller to every buyer.

(2) *Central securities depository services* means services of a clearing agency that is a securities depository as described in section 3(a)(23) of the Act.

(3) *Participant* as used in paragraphs (b)(3) and (d)(14) of this section means that if a participant controls another participant or is under common control with another participant then the affiliated participants shall be collectively deemed to be a single participant for purposes of that subparagraph.

(4) *Normal market conditions* as used in paragraphs (b)(1) and (2) of this section means conditions in which the expected movement of the price of cleared securities would produce changes in a clearing agency's exposures to its participants that would be expected to breach margin requirements or other risk control mechanisms only one percent of the time.

(5) Net capital as used in paragraph (b)(7) of this section means net capital as defined in Rule 15c3–1 under the Act for broker-dealers or any similar risk adjusted capital calculation for all other prospective clearing members.

(b) A clearing agency that performs central counterparty services shall establish, implement, maintain and enforce written policies and procedures reasonably designed to:

(1) Measure its credit exposures to its participants at least once a day and limit its exposures to potential losses from defaults by its participants in normal market conditions so that the operations of the clearing agency would not be disrupted and non-defaulting participants would not be exposed to losses that they cannot anticipate or control.

(2) Use margin requirements to limit its credit exposures to participants in normal market conditions and use risk-based models and parameters to set margin requirements and review them at least monthly.

(3) Maintain sufficient financial resources to withstand, at a minimum, a default by the participant to which it has the largest exposure in extreme but plausible market conditions; provided that a security-based swap clearing agency shall maintain sufficient financial resources to withstand, at a minimum, a default by the two participants to which it has the largest exposures in extreme but plausible market conditions.

(4) Provide for an annual model validation consisting of evaluating the performance of the clearing agency's margin models and the related parameters and assumptions associated with such models by a qualified person who does not perform functions associated with the clearing agency's margin models (except as part of the annual model validation) and does not report to a person who performs these functions.

(5) Provide the opportunity for a person that does not perform any dealer or security-based swap dealer services to obtain membership at the clearing agency to clear securities for itself or on behalf of other persons.

(6) Have membership standards that do not require that participants maintain a portfolio of any minimum size or that participants maintain a minimum transaction volume.

(7) Provide a person that maintains net capital equal to or greater than $50 million with the ability to obtain membership at the clearing agency, with any net capital requirements being scalable so that they are proportional to the risks posed by the participant's activities to the clearing agency; provided, however, that the clearing agency may provide for a higher net capital requirement as a condition for membership at the clearing agency if the clearing agency demonstrates to the Commission that such a requirement is necessary to mitigate risks that could not otherwise be effectively managed by other measures and the Commission approves the higher net capital requirement as part of a rule filing or clearing agency registration application.

(c) *Record of financial resources and annual audited financial report.* (1) Each fiscal quarter (based on calculations made as of the last business day of the clearing agency's fiscal quarter), or at any time upon Commission request, a clearing agency that performs central counterparty services shall calculate and maintain a record, in accordance with § 240.17a–1 of this chapter, of the financial resources necessary to meet the requirements of paragraph (b)(3) of this rule and sufficient documentation to explain the methodology it uses to compute such financial resource requirement.

(2) Each clearing agency shall post on its Web site an annual audited financial report. Each financial report shall:

(i) Be a complete set of financial statements of the clearing agency for the most recent two fiscal years of the clearing agency and be prepared in accordance with U.S. generally accepted accounting principles, except that for a clearing agency that is a corporation or other organization incorporated or organized under the laws of any foreign country the financial statements may be prepared in accordance with U.S. generally accepted accounting principles or International Financial Reporting Standards as issued by the International Accounting Standards Board;

(ii) Be audited in accordance with standards of the Public Company Accounting Oversight Board by a registered public accounting firm that is qualified and independent in accordance with Rule 2–01 of Regulation S–X (17 CFR 210.2–01); and

(iii) Include a report of the registered public accounting firm that complies with paragraphs (a) through (d) of Rule 2–02 of Regulation S–X (17 CFR 210.2–02).

(d) Each clearing agency shall establish, implement, maintain and enforce written policies and procedures reasonably designed to, as applicable:

(1) Provide for a well founded, transparent, and enforceable legal framework for each aspect of its activities in all relevant jurisdictions.

(2) Require participants to have sufficient financial resources and robust operational capacity to meet obligations arising from participation in the clearing agency; have procedures in place to monitor that participation requirements are met on an ongoing basis; and have participation requirements that are objective, publicly disclosed, and permit fair and open access.

(3) Hold assets in a manner whereby risk of loss or of delay in its access to them is minimized; and invest assets in instruments with minimal credit, market and liquidity risks.

(4) Identify sources of operational risk and minimize them through the development of appropriate systems, controls, and procedures; implement systems that are reliable, resilient and secure, and have adequate, scalable capacity; and have business continuity plans that allow for timely recovery of operations and fulfillment of a clearing agency's obligations.

(5) Employ money settlement arrangements that eliminate or strictly limit the clearing agency's settlement bank risks, that is, its credit and liquidity risks from the use of banks to effect money settlements with its participants; and require funds transfers to the clearing agency to be final when effected.

(6) Be cost-effective in meeting the requirements of participants while maintaining safe and secure operations.

(7) Evaluate the potential sources of risks that can arise when the clearing agency establishes links either cross-border or domestically to clear trades, and ensure that the risks are managed prudently on an ongoing basis.

(8) Have governance arrangements that are clear and transparent to fulfill the public interest requirements in section 17A of the Act applicable to clearing agencies, to support the objectives of owners and participants,

and to promote the effectiveness of the clearing agency's risk management procedures.

(9) Provide market participants with sufficient information for them to identify and evaluate the risks and costs associated with using its services.

(10) Immobilize or dematerialize securities certificates and transfer them by book entry to the greatest extent possible when the clearing agency provides central securities depository services.

(11) Make key aspects of the clearing agency's default procedures publicly available and establish default procedures that ensure that the clearing agency can take timely action to contain losses and liquidity pressures and to continue meeting its obligations in the event of a participant default.

(12) Ensure that final settlement occurs no later than the end of the settlement day; and require that intraday or real-time finality-be provided where necessary to reduce risks.

(13) Eliminate principal risk by linking securities transfers to funds transfers in a way that achieves delivery versus payment.

(14) Institute risk controls, including collateral requirements and limits to cover the clearing agency's credit exposure to each participant exposure fully, that ensure timely settlement in the event that the participant with the largest payment obligation is unable to settle when the clearing agency provides central securities depository services and extends intraday credit to participants.

(15) State to its participants the clearing agency's obligations with respect to physical deliveries and identify and manage the risks from these obligations.

5. Section 240.17Ad–23 is added to read as follows:

**§ 240.17Ad–23 Clearing agency policies and procedures to protect the confidentiality of trading information of clearing agency participants.**

Each clearing agency shall establish, implement, maintain, and enforce written policies and procedures reasonably designed to protect the confidentiality of any and all transaction information that the clearing agency receives. Such policies and procedures shall include, but are not limited to:

(a) Limiting access to confidential trading information of clearing members to those employees of the clearing agency who are operating the system or responsible for its compliance with any other applicable laws or rules; and

(b) Standards controlling employees and agents of the clearing agency trading for their personal benefit or the benefit of others.

6. Section 240.17Ad–24 is added to read as follows:

**§ 240.17Ad–24 Exemption from clearing agency definition for certain registered securities based swap dealers and registered security-based swap execution facilities.**

A registered security-based swap dealer and a registered security-based swap execution facility shall be exempt from inclusion in the term clearing agency, as defined in section 3(a)(23)(A) of the Act, where such registered security-based swap dealer or registered security-based swap execution facility would be deemed to be a clearing agency solely by reason of functions performed by such institution as part of customary dealing activities or providing facilities for comparison of data respecting the terms of settlement of securities transactions effected on such registered security-based swap execution facility, respectively, or solely by reason of acting on behalf of a clearing agency or participant therein in connection with the furnishing by the clearing agency of services to its participants or the use of services of the clearing agency by its participants.

7. Section 240.17Ad–25 is added to read as follows:

**§ 240.17Ad–25 Clearing agency procedures to identify and address conflicts of interest.**

Each clearing agency shall establish, implement, maintain and enforce written policies and procedures reasonably designed to identify and address existing or potential conflicts of interest. Such policies and procedures must also be reasonably designed to minimize conflicts of interest in decision making by the clearing agency.

8. Section 240.17Ad–26 is added to read as follows:

**§ 240.17Ad–26 Standards for board or board committee members.**

(a) Each clearing agency shall establish governance standards for its board members and board committee members.

(b) Such standards shall address at least the following areas:

(1) A clear articulation of the roles and responsibilities of directors serving on the clearing agency's board and any board committees;

(2) Director qualifications providing criteria for expertise in the securities industry, clearance and settlement of securities transactions, and financial risk management;

(3) Disqualifying factors concerning serious legal misconduct, including violations of the Federal securities laws; and

(4) Policies and procedures for the periodic review by the board or a board committee of the performance of its individual members.

9. Section 240.17Aj–1 is added to read as follows:

**§ 240.17Aj–1 Dissemination of pricing and valuation information by security-based swap clearing agencies that perform services as a central counterparty.**

Each security-based swap clearing agency that performs services as a central counterparty shall make available to the public, on terms that are fair and reasonable and not unreasonably discriminatory, all end-of-day settlement prices and any other prices with respect to security-based swaps that the clearing agency may establish to calculate mark-to-market margin requirements for its participants and any other pricing or valuation information with respect to security-based swaps as is published or distributed by the clearing agency to is participants.

Dated: March 3, 2011.

By the Commission.

**Elizabeth M. Murphy,**

*Secretary.*

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