SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–92529; File No. S7–04–21]

Order Granting Conditional Substituted Compliance in Connection With Certain Requirements Applicable to Non-U.S. Security-Based Swap Dealers and Major Security-Based Swap Participants Subject to Regulation in the United Kingdom

July 30, 2021.

I. Overview

The United Kingdom Financial Conduct Authority (''FCA'') has submitted a ''substituted compliance'' application (''FCA Application'') requesting that the Securities and Exchange Commission determine, pursuant to the Securities Exchange Act of 1934 (''Exchange Act'') rule 3a71–6,[1] that security-based swap dealers and major-security based swap participants (''SBS Entities'') subject to regulation in the United Kingdom (''UK'') conditionally may satisfy requirements under the Exchange Act by complying with comparable UK requirements.[2] The FCA Application sought substituted compliance in connection with certain Exchange Act requirements related to risk control; capital and margin; internal supervision and compliance; counterparty protection; and record keeping, reporting, notification, and securities counts.[3] The FCA Application included comparability analyses between the relevant requirements in Exchange Act section 15F and the rules and regulations thereunder and applicable UK law,[4] as well as information regarding UK supervisory and enforcement frameworks.

On April 5, 2021, the Commission issued a notice of the FCA Application, accompanied by a proposed order to grant substituted compliance with conditions in connection with the FCA Application (''proposed Order'').[5] The proposed Order incorporated a number of conditions to tailor the scope of substituted compliance consistent with the prerequisite that relevant UK requirements produce regulatory outcomes that are comparable to relevant requirements under the Exchange Act.

As discussed below, the Commission is adopting a final order (''Order'') that has been modified from the proposed Order in certain respects to address commenter concerns and to make clarifying changes.

II. Substituted Compliance Framework and Prerequisites

A. Substituted Compliance Availability and Purpose

As discussed in the UK Substituted Compliance Notice and Proposed Order, Exchange Act rule 3a71–6 provides a framework whereby non-U.S. SBS Entities may satisfy certain requirements under Exchange Act section 15F by complying with comparable regulatory requirements of a foreign jurisdiction.[6] Because substituted compliance does not constitute exemptive relief, but instead provides an alternative method by which non-U.S. SBS Entities may comply with applicable Exchange Act requirements, the non-U.S. SBS Entities would remain subject to the relevant requirements under section 15F. The Commission accordingly will retain the authority to inspect, examine, and supervise those SBS Entities' compliance and take enforcement action as appropriate. Under the substituted compliance framework, failure to comply with the applicable foreign requirements and other conditions to a substituted compliance order would lead to a violation of the applicable requirements under the Exchange Act and potential enforcement action by the Commission (as opposed to automatic revocation of the substituted compliance order).

Under rule 3a71–6, substituted compliance potentially is available in connection with certain section 15F requirements,[7] but is not available in connection with antifraud prohibitions and certain other requirements under the Federal securities laws.[8] SBS Entities in the UK accordingly must comply directly with those requirements notwithstanding the availability of substituted compliance for other requirements.

The substituted compliance framework reflects the cross-border nature of the security-based swap market, and is intended to promote efficiency and competition by helping to address potential duplication and inconsistency between relevant U.S. and foreign requirements.[9] In practice, substituted compliance may be expected to help SBS Entities leverage their existing systems and practices to comply with relevant Exchange Act requirements in conjunction with their compliance with relevant foreign requirements. Market participants will begin to count security-based swap transactions toward the thresholds for registration with the Commission as an SBS Entity on August 6, 2021, and will be required to begin registering with the

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[1] 17 CFR 240.3a71–6.

[2] *See* Letter from Nausicaa Delfas, Executive Director of International, FCA, dated March 19, 2021. The FCA Application is available on the Commission's website at: *https://www.sec.gov/files/uk-financial-conduct-authority-complete-application-substituted-compliance-031921.pdf.*

[3] ''Risk control'' includes requirements related to internal risk management, trade acknowledgment and verification, portfolio reconciliation and dispute resolution, portfolio compression, and trading relationship documentation; ''capital and margin'' includes requirements related to capital applicable to security-based swap dealers without a prudential regulator and to margin applicable to SBS Entities without a prudential regulator; ''internal supervision and compliance'' includes requirements related to diligent supervision, conflicts of interest, information gathering under Exchange Act section 15F(j), 15 U.S.C. 78*o*–10(j), and chief compliance officers; ''counterparty protection'' includes requirements related to disclosure of material risks and characteristics and material incentives or conflicts of interest, ''know your counterparty,'' suitability of recommendations, fair and balanced communications, disclosure of daily marks, and disclosure of clearing rights; and ''record keeping, reporting, notification, and securities counts'' includes requirements related to making and keeping current certain prescribed records, preservation of records, reporting, notification, and securities counts.

[4] Though the UK ceased to be a member of the European Union (''EU'') on January 31, 2020, market participants in the UK remain subject to UK requirements implemented pursuant to EU directives, and to EU regulations that have been added to UK law. In adding EU regulations to UK law, the UK in some cases has adopted UK versions of these regulations that differ from the original EU versions ''as necessary to account for the effects of Brexit.'' *See* FCA Application Appendix A at 7. The Commission has reviewed the FCA Application in light of the UK versions of these regulations.

[5] *See* Exchange Act Release No. 91476 (Apr. 5, 2021), 86 FR 18378 (Apr. 8, 2021) (''UK Substituted Compliance Notice and Proposed Order'').

[6] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18378; *see also* Exchange Act Release No. 90378 (Nov. 9, 2020), 85 FR 72726, 72727 (Nov. 13, 2020) (''German Substituted Compliance Notice and Proposed Order''); Exchange Act Release No. 90765 (Dec. 22, 2020), 85 FR 85686 (Dec. 29, 2020) (''German Substituted Compliance Order''); Exchange Act Release No. 90766 (Dec. 22, 2020), 85 FR 85720 (Dec. 29, 2020) (''French Substituted Compliance Notice and Proposed Order''); Exchange Act Release No. 91477 (Apr. 5, 2021), 86 FR 18341 (Apr. 8, 2021) (''French Substituted Compliance Re-Opening Release''); Exchange Act Release No. 92484 (Jul. 23, 2021) (''French Substituted Compliance Order'').

[7] *See* Exchange Act rule 3a71–6(d); *see also* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18378.

[8] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18378 n.5 (addressing unavailability of substituted compliance in connection with certain information-related requirements under section 15F, as well as provisions related to anti-fraud, transactions with counterparties that are not eligible contract participants, segregation of customer assets, required clearing upon counterparty election, regulatory reporting and public dissemination, SBS Entity registration, and registration of offerings).

[9] *See generally* Exchange Act Release No. 77617 (Apr. 14, 2016), 81 FR 29960, 30073 (May 13, 2016) (''Business Conduct Adopting Release'') (stating that U.S. security-based swap regulation has ''the potential to lead to requirements that are duplicative of or in conflict with applicable foreign business conduct requirements, even when the two sets of requirements implement similar goals and lead to similar results'').

Commission on November 1, 2021.[10] Substituted compliance should assist relevant non-U.S. security-based swap market participants in preparing for registration.

B. Specific Prerequisites

1. Comparability of Regulatory Outcomes

Rule 3a71–6, adopted by the Commission in 2016, describes the requirements for the Commission to make a substituted compliance determination. Under that rule, the Commission must determine that the analogous foreign requirements are comparable to otherwise applicable requirements under the Exchange Act (*i.e.,* the relevant requirements in the Exchange Act and the rules and regulations thereunder), after accounting for factors such as ''the scope and objectives of the relevant foreign regulatory requirements'' and ''the effectiveness of the supervisory compliance program administered, and the enforcement authority exercised'' by the foreign authority.[11] The comparability assessments are to be based on a ''holistic approach'' that ''will focus on the comparability of regulatory outcomes rather than predicating substituted compliance on requirement-by-requirement similarity.'' [12]

2. Memorandum of Understanding

Exchange Act rule 3a71–6(a)(2)(ii) further predicates the availability of substituted compliance on the Commission having entered into a memorandum of understanding and/or other arrangement with the relevant foreign financial regulatory authority or authorities ''addressing supervisory and enforcement cooperation and other matters arising under the substituted compliance determination.'' [13] The FCA Application asked the Commission to permit certain entities regulated and supervised by both the FCA and the UK's Prudential Regulation Authority (''PRA'') to use substituted compliance. Accordingly, the Commission recently entered into a memorandum of understanding with the FCA and the Bank of England (including in its capacity as the PRA), thus satisfying this prerequisite.[14]

3. ''Adequate Assurances''

A foreign financial regulatory authority may submit a substituted compliance application only if the authority provides ''adequate assurances'' that no law or policy would impede the ability of any entity that is directly supervised by the authority and that may register with the Commission ''to provide prompt access to the Commission to such entity's books and records or to submit to onsite inspection or examination by the Commission.'' [15] In the UK Substituted Compliance Notice and Proposed Order, the Commission stated that the FCA had satisfied this prerequisite in the Commission's preliminary view, taking into account information and representations that the FCA provided regarding certain UK requirements that are relevant to the Commission's ability to inspect, and access the books and records of, firms using substituted compliance pursuant to the Order.[16] The Commission received no comments on this preliminary view and has not changed its view.

C. Commenter Views

1. Prerequisites to Substituted Compliance

One commenter stated that the Commission should make a positive substituted compliance determination only when the Commission determines that granting substituted compliance promotes the protection of the U.S. financial system.[17] The commenter also stated that grants of substituted compliance must be predicated on a ''well-supported, evidence-based determination'' that the relevant foreign requirements will produce ''substantially similar'' regulatory outcomes.[18] Congress gave the Commission authority in Title VII to implement a security-based swap framework to address the potential effects of security-based swap activity on U.S. market participants, the financial stability of the United States, the transparency of the U.S. financial system and the protection of counterparties.[19] When adopting rules regarding the application of Title VII's definitions of ''security-based swap dealer'' and ''major security-based swap participant'' in the cross-border context, the Commission was guided by the purposes of Title VII and the applicable requirements of the Exchange Act, which include consideration of not only risk to the U.S. financial system but also other factors such as counterparty protection, transparency, prevention of evasion, economic impacts and consultation and coordination with other U.S. financial regulatory authorities and foreign financial regulatory authorities.[20] In its

[10] *See* ''Key Dates for Registration of Security-Based Swap Dealers and Major Security-Based Swap Participants,'' available at: *https://www.sec.gov/page/key-dates-registration-security-based-swap-dealers-and-major-security-based-swap-participants*.

[11] *See* Exchange Act rule 3a71–6(a)(2).

[12] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18380; *see also* Business Conduct Adopting Release, 81 FR at 30078–79 (recognizing that ''different regulatory systems may be able to achieve some or all of those regulatory outcomes by using more or fewer specific requirements than the Commission, and that in assessing comparability the Commission may need to take into account the manner in which other regulatory systems are informed by business and market practices in those jurisdictions''). The Commission's assessment of a foreign authority's supervisory and enforcement effectiveness—as part of the broader comparability analysis—would be expected to consider not only overall oversight activities, but also oversight specifically directed at conduct and activity relevant to the substituted compliance determination. ''For example, it would be difficult for the Commission to make a comparability determination in support of substituted compliance if oversight is directed solely at the local activities of foreign security-based swap dealers, as opposed to the cross-border activities of such dealers.'' Business Conduct Adopting Release, 81 FR at 30079 (footnote omitted). In the UK Substituted Compliance Notice and Proposed Order, the Commission preliminarily concluded that this comparability prerequisite was met in connection with a number of requirements under the Exchange Act, in some cases with the addition of conditions to help ensure the comparability of regulatory outcomes.

[13] Exchange Act rule 3a71–6(a)(2)(ii).

[14] The Commission expects to publish a copy of the memorandum of understanding on its website at *www.sec.gov* under the ''Substituted Compliance'' tab, which is located on the ''Security-Based Swap Markets'' page in the Division of Trading and Markets section of the site.

[15] *See* Exchange Act rule 3a71–6(c)(3).

[16] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18379 n.8.

[17] *See* Letter from Dennis M. Kelleher, President and CEO, Stephen Hall, Legal Director and Securities Specialist, and Jason Grimes, Senior Counsel, Better Markets, Inc. (May 3, 2021) (''Better Markets Letter'') at 3–4. Comments may be found on the Commission's website at: *https://www.sec.gov/comments/s7-04-21/s70421.htm*.

[18] *See* Better Markets Letter at 4.

[19] *See* Exchange Act Release No. 72472 (June 25, 2014), 79 FR 47278, 47286 (Aug. 12, 2014) (''Cross-Border Entity Definitions Adopting Release'') (citing Pub. L. 111–203, Preamble (stating that the Dodd-Frank Act was enacted ''[t]o promote the financial stability of the United States by improving accountability and transparency in the financial system, to end 'too big to fail', to protect the American taxpayer by ending bailouts, to protect consumers from abusive financial services practices, and for other purposes''); Public Law 111–203, sections 701–774 (providing for, among other things, a comprehensive new regulatory framework for security-based swaps, including by: (i) Providing for the registration and comprehensive regulation of security-based swap dealers and major security-based swap participants; (ii) imposing clearing and trade execution requirements on security-based swaps, subject to certain exceptions; and (iii) creating real-time reporting and public dissemination regimes for security-based swaps)).

[20] *See* Cross-Border Entity Definitions Adopting Release, 79 FR at 47292 (purposes of Title VII include consideration of risk to the U.S. financial system and promotion of transparency in the U.S. financial system); Exchange Act section 30(c), 15 U.S.C. 78dd(c) (Commission rulemaking authority to prevent evasion of Title VII); Exchange Act section 3(f), 15 U.S.C. 78c(f) (requirement to consider whether certain Commission rulemaking

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registration rules for these SBS Entities, the Commission determined that a foreign market participant whose U.S.-nexus security-based swap activity qualifies it as an SBS Entity would be required to register as such, without substituted compliance available for registration requirements.[21] The Commission concluded that obliging these foreign persons to register serves an important regulatory function that would be significantly impaired by permitting substituted compliance for registration requirements.[22] This registration requirement thus puts into practice the Commission's consideration of the purposes of Title VII and the applicable requirements of the Exchange Act in its adoption of the definitions of ''security-based swap dealer'' and ''major security-based swap participant'' in the cross-border context, and ensures that such firms will be subject to the jurisdiction of the Commission. Moreover, the rules applicable to these registered foreign SBS Entities reflect the Commission's best judgment for how to achieve the purposes of Title VII and satisfy the requirements of the Exchange Act, including the Commission's consideration of risk to the U.S. financial system.[23] The Commission's rules for registered foreign SBS Entities thus reflect the Commission's consistent consideration of all of the purposes of Title VII and relevant parts of the Exchange Act, first in the context of its adoption of the definitions of ''security-based swap dealer'' and ''major security-based swap participant,'' then in its decision to require foreign SBS Entities to register and finally in its adoption of cross-border rules for SBS Entities pursuant to Title VII.

When making a substituted compliance determination, the Commission's task, as outlined in rule 3a71–6, is to evaluate whether the relevant foreign requirements are comparable to Title VII-based requirements and relevant provisions of the Exchange Act. The comparability assessments are to be based on a ''holistic, outcomes-oriented framework,'' [24] which in the Commission's view—consistent with the commenter's view—includes ''inquiry regarding whether foreign requirements adequately reflect the interests and protections associated with the particular Title VII requirement.'' [25] Also consistent with the commenter's view, the Commission's comparability assessments reflect a close reading of the relevant UK requirements. In addition, the Commission recognizes that ''other regulatory regimes will have exclusions, exceptions, and exemptions that may not align perfectly with the corresponding requirements under the Exchange Act.'' [26] Accordingly, where UK requirements produce comparable outcomes—with or without conditions as discussed in part III.B below—notwithstanding those particular differences, and taking into account the scope and objectives and the effectiveness of supervision and enforcement of those requirements, the Commission has determined that the relevant UK requirements are comparable and has made a positive substituted compliance determination. Conversely, where those exclusions, exemptions, and exceptions lead to outcomes that are not comparable—taking into account potential conditions—the Commission has not made a positive substituted compliance determination.

The Commission also is including certain conditions in the Order. The commenter stated that the inclusion of conditions should be viewed as an indication that the requirements of substituted compliance have not been met and as creating ''ad hoc, custom-made rules to supplement inadequate rules of other jurisdictions.'' [27] Pursuant to rule 3a71–6, the Commission may make a conditional or unconditional substituted compliance determination.[28] As described in greater detail in part III.B below, many of the conditions in the Order are designed to make substituted compliance available only when the relevant UK requirements in fact apply to the relevant security-based swap activity in a way that promotes comparable regulatory outcomes. The commenter correctly states that the Order also employs conditions to promote comparability. For example, substituted compliance in connection with Exchange Act rule 15Fi–3(c) [29] dispute reporting provisions is conditioned in part on the Covered Entity (as such term is defined in the Order) providing the Commission with the dispute reports required under UK law.[30] Consistent with rule 3a71–6, conditioning substituted compliance on the Commission receiving those reports helps to promote timely notice of disputes to support a comparable regulatory outcome.

2. Ensuring Ongoing Appropriateness of Substituted Compliance

One commenter stated that the Commission ''must ensure, on an ongoing basis, that each grant of substituted compliance remains appropriate over time.'' The commenter added that substituted compliance orders and memoranda of understanding should incorporate the obligation that the Commission be apprised of the activities and results of the jurisdiction's supervision and enforcement programs, and to immediately apprise the Commission of

actions would promote efficiency, competition, and capital formation); Exchange Act section 23(a)(2), 15 U.S.C. 78w(a)(2) (requirement to consider the impact of Exchange Act rules and regulations on competition and prohibition on adopting rules or regulations that would impose a burden on competition not necessary or appropriate in furtherance of the purposes of the Exchange Act); Dodd-Frank Act section 712(a)(2), 15 U.S.C. 8302 (requirement to consult and coordinate with U.S. financial regulatory authorities on Title VII rulemaking); Dodd-Frank Act section 752(a), 15 U.S.C. 8325 (requirement to consult and coordinate, as appropriate, with foreign regulatory authorities on the establishment of consistent international standards with respect to the regulation of security-based swaps and security-based swap entities)); *see also* Exchange Act Release No. 77104 (Feb. 10, 2016), 81 FR 8598, 8599 (Feb. 19, 2016) (''ANE Adopting Release'') (''A key part of [the Title VII] framework is the regulation of security-based swap dealers, which may transact extensively with counterparties established or located in other jurisdictions and, in doing so, may conduct sales and trading activity in one jurisdiction and book the resulting transactions in another. These market realities and the potential impact that these activities may have on U.S. persons and potentially the U.S. financial system have informed our consideration of these rules.''); Exchange Act Release No. 87780 (Dec. 18, 2019), 85 FR 6270, 6272 and n.26 (Feb. 4, 2020) (''Cross-Border Adopting Release'') (''[T]he Title VII SBS Entity requirements . . . serve a number of regulatory purposes apart from mitigating counterparty and operational risks, 'including enhancing counterparty protections and market integrity, increasing transparency, and mitigating risk to participants in the financial markets and the U.S. financial system more broadly.' '' ''The Commission's actions to mitigate the negative consequences potentially associated with the various uses of [the 'arranged, negotiated, or executed' test] accordingly are designed to do so while preserving the important Title VII interests that the Commission advanced when it incorporated the test into the various cross-border rules.'') (internal citations omitted).

[21] *See* Exchange Act Release No. 75611 (Aug. 5, 2015), 80 FR 48964, 48972–73 (Aug. 14, 2015) (''Registration Adopting Release'').

[22] *See* Registration Adopting Release, 80 FR at 48972–73.

[23] *See* Cross-Border Entity Definitions Adopting Release, 79 FR at 47286 n.65 (''Future rulemakings that depend on [the definitions of 'security-based swap dealer' and 'major security-based swap participant'] are intended to address the transparency, risk, and customer protection goals of Title VII.'').

[24] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18380; *see also* Business Conduct Adopting Release, 81 FR at 30076, 30078–79.

[25] *See* Business Conduct Adopting Release, 81 FR at 30067.

[26] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18380; *see also* Business Conduct Adopting Release, 81 FR at 30076, 30078–79.

[27] *See* Better Markets Letter at 4.

[28] *See* Exchange Act rule 3a71–6(a)(1).

[29] 17 CFR 240.15Fi–3(c).

[30] *See* para. (b)(3)(ii) of the Order.

material changes to the foreign regulatory regime.[31]

The Commission concurs that the ongoing availability of substituted compliance should account for relevant changes in the foreign jurisdiction's regulatory requirements and in the effectiveness of that jurisdiction's supervisory and enforcement program.[32] Accordingly, the Commission and the FCA and the Bank of England in its capacity as the PRA recently entered into a substituted compliance memorandum of understanding that addresses ongoing information regarding potential changes to substantive legal requirements and supervisory and enforcement effectiveness.[33] The Commission believes that these arrangements will provide timely information to ensure that the Commission is aware of material developments that may affect the comparability of the relevant UK requirements, including the scope and objectives of those requirements and the effectiveness of the FCA and the Bank of England's supervision and enforcement programs. In response to any such developments, the Commission may amend the Order as needed to ensure that it continues to require a Covered Entity to comply with comparable UK requirements, or may withdraw the Order if the relevant UK requirements are no longer comparable.[34] Moreover, substituted compliance under the Order is conditioned on the Commission having this memorandum of understanding, or another arrangement with the FCA and the Bank of England addressing cooperation with respect to the Order, at the time the Covered Entity makes use of substituted compliance.[35] If the arrangements in the memorandum of understanding prove in practice not to provide information about relevant developments, the Commission could terminate the memorandum of understanding in accordance with its terms and/or amend or withdraw the Order.[36] If the Commission, the FCA, or the Bank of England terminates the memorandum of understanding, Covered Entities would not be able to rely on substituted compliance under the Order to satisfy Exchange Act compliance obligations that arise after the termination takes effect. For these reasons, in the Commission's view, the Order's memorandum of understanding condition, coupled with the ongoing information sharing provisions in the memorandum of understanding with the FCA and the Bank of England, establishes the commenter's suggested mechanism to apprise the Commission of changes that may affect the ongoing appropriateness of substituted compliance.

III. General Availability of Substituted Compliance Under the Order

A. Covered Entities

1. Proposed Approach

Under the proposed Order, the definition of ''Covered Entity'' specified which entities could make use of substituted compliance. Consistent with the availability of substituted compliance under Exchange Act rule 3a71–6, the proposed definition in part would limit the availability of substituted compliance to registered SBS Entities that are not U.S. persons. In addition, to help ensure that firms that rely on substituted compliance are subject to relevant UK requirements and oversight, the proposed definition would require that a Covered Entity is a ''MiFID investment firm'' or ''third country investment firm,'' as such terms are defined in the FCA Handbook Glossary, that (a) has permission from the FCA or PRA under Part 4A of the UK's Financial Services and Markets Act 2000 (''FSMA'') to carry on regulated activities relating to investment services and activities in the UK; (b) is supervised by the FCA under the fixed supervision model; and (c) if the firm is a PRA-authorized person, also is supervised by the PRA as a Category 1 firm.[37]

2. Final Provisions

Commenters did not address the proposed ''Covered Entity'' definition, and the Commission is issuing the definition as proposed.[38] Substituted compliance accordingly is available only to non-U.S. SBS Entities that have the relevant UK regulatory permission and are subject to UK oversight.

B. Additional General Conditions and Other Prerequisites

1. Proposed Approach

The proposed Order incorporated a number of additional general conditions and other prerequisites, to help ensure that the relevant UK requirements that form the basis for substituted compliance in practice will apply to the Covered Entity's security-based swap business and activities, and to promote the Commission's oversight over entities that avail themselves of substituted compliance:

- ''*Subject to and complies with*'' *applicability condition*—For each relevant section of the proposed Order, a positive substituted compliance determination would be subject to the condition that the Covered Entity be subject to and comply with the applicable UK requirements needed to establish comparability.[39]
- ''*Regulated activities*''—For each condition in the proposed Order that requires the application of, and compliance with, provisions of the Senior Management Arrangements, Systems and Controls Sourcebook of the FCA Handbook (''FCA SYSC'') 4, 5, 6, 7, 9, and/or 10, certain parts of the PRA Rulebook and/or MLR 2017, the Covered Entity's relevant security-based swap activities must constitute ''regulated activities'' as defined for purposes of the relevant UK provisions, must be carried on by the Covered Entity from an establishment in the UK and must fall within the scope of the Covered Entity's authorization from the FCA and/or PRA to conduct regulated activities in the UK.[40]
- *UK MiFID* ''*investment services or activities*''—For each condition in the proposed Order that requires the application of, and compliance with, provisions of the Product Intervention and Product Governance Sourcebook of the FCA Handbook (''FCA PROD'') 3 and/or the UK version of Commission Delegated Regulation (EU) 2017/565

[31] *See* Better Markets Letter at 5.

[32] *See* Business Conduct Adopting Release, 81 FR at 30078–79 (stating that order conditions and memorandum of understanding were possible tools for providing that the Commission be notified of material changes).

[33] The memorandum of understanding between the Commission and the FCA and the Bank of England in part provides that the FCA and the Bank of England will provide ''ongoing information sharing'' regarding Firm Information (incorporating supervisory and related information as to the Covered Entities using substituted compliance) and regarding Regulatory Change Information (incorporating information about any material publicly available draft, proposed, or final change in law, regulation, or order of the jurisdiction of the FCA or the Bank of England that may have a material impact on the firms at issue with respect to their relevant activities). *See supra* note 14 (information on publication of memorandum of understanding with the FCA and the Bank of England).

[34] Any such amendment or withdrawal may be at the Commission's own initiative after appropriate notice and opportunity for comment. *See* Exchange Act rule 3a71–6(a)(3).

[35] *See supra* part II.B.2; para. (a)(15) of the Order.

[36] *See supra* note 14.

[37] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18380.

[38] *See* para. (g)(1) of the Order.

[39] The Commission stated, as an example, that this proposed condition would not be satisfied when the comparable UK requirements would not apply to the security-based swap activities of a non-UK branch of a MiFID investment firm or to a third country investment firm. *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18380.

[40] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18381.

(''UK MiFID Org Reg''), the Covered Entity's relevant security-based swap activities must constitute ''investment services or activities,'' as defined in the FCA Handbook Glossary, must be carried on by the Covered Entity from an establishment in the UK and must fall within the scope of the Covered Entity's authorization from the FCA and/or PRA to conduct regulated activities in the UK.[41]

• *UK* ''*MiFID or equivalent third country business*''—For each condition in the proposed Order that requires the application of, and compliance with, provisions of the Conduct of Business Sourcebook of the FCA Handbook (''FCA COBS'') 2, 4, 6, 8A, 9A, 14, and/or 14A, the Covered Entity's relevant security-based swap activities must constitute ''MiFID or equivalent third country business,'' as defined in the FCA Handbook Glossary, must be carried on by the Covered Entity from an establishment in the UK and must fall within the scope of the Covered Entity's authorization from the FCA and/or PRA to conduct regulated activities in the UK.[42]

• *UK* ''*designated investment business*''—For each condition in the proposed Order that requires the application of, and compliance with, provisions of FCA COBS 11, the Covered Entity's relevant security-based swap activities must constitute ''MiFID business'' that is also ''designated investment business,'' each as defined in the FCA Handbook Glossary, must be carried on by the Covered Entity from an establishment in the UK and must fall within the scope of the Covered Entity's authorization from the FCA and/or PRA to conduct regulated activities in the UK.[43]

• *UK* ''*MiFID business*''—For each condition in the proposed Order that requires the application of, and compliance with, provisions of the Client Asset Sourcebook of the FCA Handbook (''FCA CASS'') 6 and/or 7, the Covered Entity must not be an ''investment company with variable capital'' as defined in the FCA Handbook Glossary,[44] the Covered Entity's relevant security-based swap activities must constitute ''regulated activities'' as defined for purposes of the relevant UK provisions and ''MiFID business'' as defined in the FCA Handbook Glossary, must be carried on by the Covered Entity from an establishment in the UK and must fall within the scope of the Covered Entity's authorization from the FCA and/or PRA to conduct regulated activities in the UK.[45]

• *Activities covered by FCA SYSC 10A*—For each condition in the proposed Order that requires the application of, and compliance with, provisions of FCA SYSC 10A, the Covered Entity's relevant security-based swap activities must constitute activities described in FCA SYSC 10A.1.1(2)(a), (b) and/or (c), must be carried on by the Covered Entity from an establishment in the UK and must fall within the scope of the Covered Entity's authorization from the FCA and/or PRA to conduct regulated activities in the UK.[46]

• *UK MiFID* ''*clients*''—For each condition in the proposed Order that requires the application of, and compliance with, provisions of FCA CASS 6 and/or 7, FCA COBS 2, 4, 6, 8A, 9A, 11, 14, and/or 14A, FCA PROD 3, FCA SYSC 10.1.8, FCA SYSC 10A, and/or UK MiFID Org Reg, the Covered Entity's relevant counterparties (or potential counterparties) must be ''clients'' (or potential ''clients'') as defined in FCA COBS 3.2.1R.[47]

• *UK MiFID* ''*financial instruments*''—For each condition in the proposed Order that requires the application of, and compliance with, provisions of FCA CASS 6 and/or 7, FCA COBS 2, 4, 6, 8A, 9A, 11, 14, and/or 14A, FCA PROD 3, FCA SYSC 10A, the UK version of Market Abuse Regulation (EU) 596/2014 (''UK MAR''), the UK version of Commission Delegated Regulation (EU) 2016/958 (''UK MAR Investment Recommendations Regulation''), and/or UK MiFID Org Reg, the relevant security-based swap must be a ''financial instrument'' as defined in Part 1 of Schedule 2 of the UK Regulated Activities Order.[48]

• *UK CRD/CRR* ''*institution*''—For each condition in the proposed Order that requires the application of, and compliance with, provisions of the UK version of the Capital Requirements Regulation, Regulation (EU) No 575/2013 (''UK CRR''), the Covered Entity must be an ''institution'' as defined in UK CRR article 4(1)(3).[49]

• ''*Common platform firm*'' *or* ''*third country firm*''—For each condition in the proposed Order that requires the application of, and compliance with, provisions of FCA SYSC 4, 5, 6, 7, 9, and/or 10, the Covered Entity must be either a ''common platform firm'' (other than a ''UCITS investment firm'') or a ''third country firm,'' each as defined in the FCA Handbook Glossary.[50]

• ''*IFPRU investment firm*''—For each condition in the proposed Order that requires the application of, and compliance with, provisions of FCA SYSC 19A, the Prudential Sourcebook for Investment Firms of the FCA Handbook (''FCA IFPRU''), and/or the Prudential Sourcebook for Banks, Building Societies and Investment Firms of the FCA Handbook (''FCA BIPRU''), the Covered Entity must be an ''IFPRU investment firm'' as defined in the FCA Handbook Glossary.[51]

• ''*UK bank*'' *or* ''*UK designated investment firm*''—For each condition in the proposed Order that requires the application of, and compliance with, provisions of FCA SYSC 19D and/or certain parts of the PRA Rulebook, the Covered Entity must be a ''UK bank'' or ''UK designated investment firm,'' each as defined in the FCA Handbook Glossary (in the case of chapter 19D of FCA SYSC) or in the PRA Rulebook Glossary (in the case of a part of the PRA Rulebook).[52]

• *Covered Entity's counterparties as UK EMIR* ''*counterparties*''—For each condition in the proposed Order that requires the application of, and compliance with, provisions of the UK version of the European Market Infrastructure Regulation (''EMIR''), Regulation (EU) No 648/2012 (''UK EMIR''), the UK version of Commission Delegated Regulation (EU) No 149/2013 (''UK EMIR RTS''), and/or the UK version of Commission Delegated Regulation (EU) 2016/2251 (''UK EMIR Margin RTS''), if the counterparty to the Covered Entity is not a ''financial counterparty'' or ''non-financial counterparty'' as defined in UK EMIR articles 2(8) or 2(9), respectively, the

[41] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18381.

[42] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18381. In the final Order, the Commission has corrected the typographical error in paragraph (a)(3) by changing FCA COBS 14A to 16A. *See* para. (a)(3) of the Order.

[43] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18381.

[44] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18381.

[45] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18381.

[46] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18381.

[47] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18381. In the final Order, the Commission has corrected the typographical error in paragraph (a)(7) by changing FCA COBS 14A to 16A. *See* para. (a)(7) of the Order.

[48] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18381–82. In the final Order, the Commission has corrected the typographical error in paragraph (a)(8) by changing FCA COBS 14A to 16A. *See* para. (a)(8) of the Order.

[49] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18382.

[50] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18382.

[51] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18382.

[52] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18382.

Covered Entity must comply with the applicable condition as if the counterparty were a financial counterparty or non-financial counterparty. If the Covered Entity reasonably determines that the counterparty conducts a financial business that would cause it to be a financial counterparty if it were UK-established and UK-authorized, then the proposed Order would require the Covered Entity to treat the counterparty as a financial counterparty; otherwise, the proposed Order would require the Covered Entity to treat the counterparty as a non-financial counterparty. In addition, the proposed Order would provide that a Covered Entity complying with UK EMIR could not apply substituted compliance by complying with third country requirements that UK authorities may determine to be equivalent to UK EMIR.[53]

• *Security-based swap status under UK EMIR*—For each condition in the proposed Order that requires the application of, and compliance with, provisions of UK EMIR, UK EMIR RTS, and/or UK EMIR Margin RTS, either: (1) The relevant security-based swap must be an ''OTC derivative'' or ''OTC derivative contract,'' as defined in UK EMIR article 2(7), that has not been cleared by a central counterparty and otherwise is subject to the provisions of UK EMIR article 11, UK EMIR RTS articles 11 through 15, and UK EMIR Margin RTS article 2; or (2) the relevant security-based swap must have been cleared by a central counterparty that has been authorized or recognized to clear derivatives contracts in the UK.[54]

• *Memorandum of understanding*—Consistent with the requirements of rule 3a71–6 and the Commission's need for access to information regarding registered entities, substituted compliance under the proposed Order would be conditioned on the Commission having an applicable memorandum of understanding or other arrangement with the FCA and the PRA addressing cooperation with respect to the Order at the time the Covered Entity makes use of substituted compliance.[55]

• *Notice of reliance on substituted compliance*—To assist the Commission's oversight of firms that avail themselves of substituted compliance, a Covered Entity relying on the Order would have to provide notice of its intent to rely on the Order by notifying the Commission in writing. In the notice, the Covered Entity would need to identify each specific substituted compliance determination in the Order for which the Covered Entity intends to apply substituted compliance. The Covered Entity would have to promptly update the notice if it intends to modify its reliance on substituted compliance.[56]

2. Commenter Views and Final Provisions

One commenter expressed general support for several of the general conditions, subject to certain changes and clarifications.[57] Another commenter stated that, if the Commission makes a positive substituted compliance determination, it must ensure that the conditions in the proposed Order are applied ''with full force and without exception or dilution.[58] The Commission is issuing the general conditions largely as proposed,[59] and details its responses to the requested changes and clarifications below. In the Commission's view, the conditions are structured appropriately to predicate a positive substituted compliance determination on the applicability of relevant UK requirements needed to establish comparability, as well as on the continued effectiveness of the requisite memorandum of understanding, and the provision of notice to the Commission regarding the Covered Entity's intent to rely on substituted compliance.

a. UK Territorial Condition

A commenter stated that the Commission should delete the requirement in paragraphs (a)(1) through (a)(6) of the Order that, for purposes of certain UK requirements, a Covered Entity's relevant security-based swap activities be ''carried on . . . from an establishment in the United Kingdom.'' [60] The commenter stated that this UK territorial aspect of the conditions was not necessary because some of the UK requirements listed in these conditions apply to a Covered Entity with respect to activities wherever they are carried on.[61] The commenter suggested that the Commission instead add a new general condition that would require a Covered Entity, when relying on a part of the Order that requires it to be subject to and comply with the UK requirements listed in paragraphs (a)(1) through (a)(6) of the Order, to carry on the relevant security-based swap activities from a UK establishment, but only to the extent that those UK requirements ''are limited in their applicability to activity carried on from [a UK establishment].'' [62] The commenter did not identify any specific instances in which it believes that a Covered Entity would carry on a particular security-based swap activity outside the United Kingdom and that activity would be subject to the UK requirements listed in paragraphs (a)(1) through (a)(6) of the Order.

Many, though not all, of these UK requirements contain clearly articulated scoping provisions that apply the requirements to Covered Entities only when the relevant activity is carried on from an establishment in the UK.[63] Other requirements contain more complex scoping provisions, and the Commission is aware that in limited cases it is possible for these requirements to apply to some aspects of a Covered Entity's activities carried on from an establishment outside the UK. For example, the FCA commented that certain organizational requirements generally apply in a prudential context to activities wherever they are carried on.[64] In addition, PRA General

[53] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18382.

[54] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18382.

[55] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18382. The Commission has entered into a memorandum of understanding with the FCA and the PRA to address substituted compliance cooperation. *See supra* note 14. Consistent with the final Order, Covered Entities must ensure that this memorandum of understanding remains in place at the time the Covered Entity relies on substituted compliance.

[56] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18382.

[57] *See* Letter from Kyle L. Brandon, Managing Director, Head of Derivatives Policy, SIFMA (May 3, 2021) (''SIFMA 5/3/2021 Letter'') at 3–9.

[58] *See* Better Markets Letter at 2.

[59] *See* paras. (a)(1) through (16) of the Order. The Commission is correcting typographical errors in paragraphs (a)(3), (a)(7), and (a)(8) of the Order by replacing references to FCA COBS 14A with references to FCA COBS 16A.

[60] *See* SIFMA 5/3/2021 Letter at 3–4.

[61] *See* SIFMA 5/3/2021 Letter at 3.

[62] *See* SIFMA 5/3/2021 Letter at 3–4 and Appendix A. Together with its request to amend the UK territorial condition in paragraphs (a)(1) through (a)(6) of the Order, the commenter requested that the Commission delete, where feasible, references to compliance with territorially limited UK laws as conditions to substituted compliance. *See* SIFMA 5/3/2021 Letter at 4. The Commission addresses this additional request below in the relevant parts of this release.

[63] *See* FCA SYSC 1 Annex 1 2.15R (The common platform requirements, which include FCA SYSC 4, 5, 6, 7, and 10, apply in relation to activities carried on from an establishment in the UK.); FCA SYSC 10A.1.1R(2) (FCA SYSC 10A applies only to activities carried on from an establishment in the UK.); Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 (''MLR 2017'') Regulation 8 (The relevant requirements of MLR 2017 apply to persons acting in the course of business carried on by them in the UK.); FCA CASS 1.3.2R (FCA CASS 6 and 7 apply to regulated activities carried on from an establishment in the UK.).

[64] *See* comments from FCA (May 20, 2021) (''FCA Comments'') (noting that common platform organizational requirements, including FCA SYSC 4 to 9, and parallel PRA General Organisational Requirements, generally apply in a prudential context to activities wherever they are carried on).

Organisational Requirements, PRA Recordkeeping Rules, PRA Risk Control Rules, and PRA Remuneration Rules generally apply to a Covered Entity that is a ''CRR firm'' with respect to activities carried on from a UK establishment,[65] but also apply to activities anywhere in the world ''in a prudential context,'' [66] which the PRA defines to mean when the Covered Entity's activities have, or might reasonably be regarded as likely to have, a negative effect on the Covered Entity's safety and soundness or its ability to continue to meet certain other UK regulatory tests.[67] The Commission cannot, however, determine *ex ante* whether a Covered Entity's particular activity outside the UK would fall within these limited wider scope provisions. The commenter also did not identify any circumstances that would trigger the limited wider scope of these provisions. Moreover, it is unclear whether any such wider scope even would be relevant in the context of the Order or, if so, how that wider scope would impact the operation of the Order in practice. For these reasons, the Commission is retaining the requirement in paragraph (a)(1) of the Order for the Covered Entity to carry on the relevant activities from an establishment in the UK.[68]

Other UK requirements listed in paragraphs (a)(2) through (a)(4) of the Order apply to limited activities outside the UK for which a Covered Entity might apply substituted compliance. UK MiFID Org Reg generally applies to a Covered Entity that is a third country investment firm only when it carries on the relevant security-based swap activity from an establishment in the UK,[69] but provisions of UK MiFID Org Reg in some instances can apply to a broader range of activities if the Covered Entity is a MiFID investment firm. Similarly, FCA PROD 3 and FCA COBS generally apply to a Covered Entity with respect to activities carried on from an establishment in the UK,[70] but also apply to a Covered Entity with respect to certain activities with a client in the UK that are carried on from an establishment outside the UK.[71] The Commission is amending the general conditions in paragraphs (a)(2) through (a)(4) of the Order to provide that a Covered Entity's relevant security-based swap activities must be either carried on by the Covered Entity from an establishment in the UK or from any other place that would cause UK MiFID Org Reg, FCA PROD 3, and/or the relevant provision(s) of FCA COBS, as applicable, to apply to those activities.

In applying these amended general conditions, a Covered Entity still must satisfy all of the applicable general conditions, as well as the other applicable provisions of the Order, relating to a particular Exchange Act requirement for which it applies substituted compliance. A Covered Entity will satisfy the conditions of the Order only when it is subject to and complies with all of the comparable UK requirements listed in the relevant provision(s) of the Order. If any one of these comparable UK requirements is subject to a general condition with a territorial limitation, the relevant security-based swap activity for which the Covered Entity applies substituted compliance would have to satisfy that territorial limitation, even if another of the comparable UK requirements applies to a wider scope of activities. As a result, in these instances a Covered Entity would be able to use substituted compliance only for security-based swap activities that satisfy the territorial limitation.

b. Scope of Substituted Compliance

The same commenter requested that the Commission delete, where feasible, references in the Order to territorially limited UK requirements.[72] Where these deletions are not feasible, the commenter requested that the Commission confirm that, in relation to entity-level Exchange Act requirements, a Covered Entity may (a) rely on substituted compliance for its relevant security-based swap activities carried on from an establishment in the UK and (b) comply with Exchange Act requirements or another applicable substituted compliance order for its relevant security-based swap activities carried on from an establishment outside the UK.[73] The Commission is addressing here the commenter's request for clarification of the availability of substituted compliance for entity-level Exchange Act requirements, and is addressing the commenter's various requested deletions below in the relevant parts of this release.[74]

In the proposed Order, the Commission stated that a Covered Entity applying substituted compliance for one or more entity-level Exchange Act requirements (including risk control, capital, margin, internal supervision and chief compliance officer requirements, as well as recordkeeping and reporting requirements other than those linked to counterparty protection requirements) would have to apply substituted compliance at an entity level, *i.e.,* to all of its activities subject to that particular Exchange Act requirement.[75] By contrast, the Commission stated that a Covered Entity applying substituted compliance for one or more transaction-level Exchange Act requirements (including counterparty protection requirements, as well as recordkeeping and reporting requirements linked to them) could choose to apply substituted compliance under the proposed Order for some activities and comply directly with Exchange Act requirements for other activities.[76] The proposed Order thus would provide substituted compliance for transaction-level Exchange Act requirements ''in relation to [a specific security-based swap, counterparty, recommendation, or communication];'' the proposed Order did not include this proviso in relation to substituted compliance for entity-level Exchange Act requirements.[77] The Commission proposed this approach in the context of assisting Covered Entities in choosing between applying substituted compliance pursuant to the Order or complying directly with relevant Exchange Act requirements. This approach did not address, and does not

[65] *See* PRA General Organisational Requirements Rule 1.1(1); PRA Recordkeeping Rule 1.1(1); PRA Risk Control Rule 1.1(1); *see also* PRA Remuneration Rule 1.1(1)(a) (PRA Remuneration Rules apply to a CRR firm in relation to its ''UK activities.'').

[66] *See* PRA General Organisational Requirements Rule 1.1(3); PRA Recordkeeping Rule 1.1(3); PRA Risk Control Rule 1.1(3); PRA Remuneration Rule 1.1(c).

[67] *See* PRA Rulebook Glossary.

[68] The Commission also is retaining the same requirement in paragraphs (a)(5) and (a)(6) of the Order, as the UK requirements referenced in those paragraphs apply only to activities carried on from an establishment in the UK.

[69] *See* General Provisions Sourcebook of the FCA Handbook (''FCA GEN'') 2.2.22AR.

[70] *See* FCA PROD 1.3.4R.

[71] *See* FCA PROD 1.3.5R(1) (general UK territorial rule for FCA PROD 3); FCA COBS 4.1.8R (general UK territorial rule for FCA COBS 4) (citing FCA COBS 1.1.1R); *but see* FCA PROD 1.3.5(2) (exclusions from FCA PROD 3 for activities from an establishment outside the UK); FCA COBS 1 Annex 1 Part 2 2.1R (exclusions from FCA COBS 4 for activities from an establishment outside the UK).

[72] *See* SIFMA 5/3/2021 Letter at 4.

[73] *See* SIFMA 5/3/2021 Letter at 4.

[74] *See infra* parts IV.B, V.B, VI.B, VII.B, and VIII.B.

[75] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18384 (risk control requirements), 18386–87 (capital and margin requirements), 18389–90 (internal supervision and chief compliance officer requirements), 18395–96 (recordkeeping, reporting, notification, and securities count requirements other than those linked to counterparty protection requirements).

[76] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18392 (counterparty protection requirements), 18396 (recordkeeping and reporting requirements linked to counterparty protection requirements).

[77] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18413–20.

apply to, security-based swap business for which a Covered Entity could not apply substituted compliance under the proposed Order because the Covered Entity is not subject to the relevant UK requirements listed in the Order with respect to that business.[78]

Consistent with the commenter's request, for any particular set of entity-level Exchange Act requirements,[79] a Covered Entity must choose either (1) to apply substituted compliance pursuant to the Order with respect to all security-based swap business that is subject to the relevant UK requirements listed in the Order and that can satisfy any general conditions related to those UK requirements (including any applicable UK territorial condition) (''UK business''), or (2) to comply directly with the Exchange Act with respect to all UK business. A Covered Entity may not choose to apply substituted compliance for those entity-level requirements in respect of some of its UK business and comply directly with the Exchange Act in respect of another part of its UK business. However, if the conditions in the relevant part of the Order require the Covered Entity to comply with UK requirements that are subject to a UK territorial condition, the Covered Entity's UK business would not include business carried on from an establishment outside the UK, as that business would not be subject to the relevant UK requirements and would not satisfy the applicable UK territorial condition. Rather, the Covered Entity could apply substituted compliance for the Exchange Act requirements in that part of the Order so long as it applies substituted compliance for all of its business that is subject to the relevant UK requirements and can satisfy any general conditions related to those UK requirements, which in this example would include only business that is carried on from an establishment in the UK and that otherwise is both subject to the relevant UK requirements and able to satisfy any other general conditions related to those requirements. Also consistent with the commenter's request, for any particular set of entity-level Exchange Act requirements, if the Covered Entity also has security-based swap business that is not subject to the relevant UK requirements [80] or that cannot satisfy an applicable general condition related to those UK requirements (including business carried on from an establishment outside the UK where the Order imposes a UK territorial condition) the Covered Entity must either comply directly with the Exchange Act for that business or comply with the terms of another applicable substituted compliance order.[81] Consistent with the proposed Order, for transaction-level Exchange Act requirements, a Covered Entity may decide to apply substituted compliance for some of its security-based swap business and to comply directly with the Exchange Act (or comply with another applicable substituted compliance order) for other parts of its security-based swap business.[82] The Commission believes that this scope of substituted compliance strikes the right balance to ensure that substituted compliance is consistent with Commission's classification of Exchange Act requirements as either entity-level or transaction-level requirements. The Commission has made no changes to the text of the Order in connection with these issues.

In the Covered Entity's notice to the Commission pursuant to paragraph (a)(16) of the Order, the Covered Entity must specify the parts of its security-based swap business for which it will apply substituted compliance consistent with the individual parts of the Order. Every SBS Entity registered with the Commission, whether complying directly with Exchange Act requirements or relying on substituted compliance as a means of complying with the Exchange Act, is required to satisfy the inspection and production requirements imposed on such entities under the Exchange Act,[83] and specificity as to the scope of the entity's reliance on substituted compliance is

[78] For example, this approach did not address and would not apply to a Covered Entity's security-based swap business carried on from an establishment outside the UK, when the relevant part of the proposed Order would require the Covered Entity to comply with one or more UK requirements to which a UK territorial condition applies.

[79] A Covered Entity may use substituted compliance consistent with the Order for any one or more sets of entity-level Exchange Act requirements specified in the Order. *See supra* note 74 and accompanying text. For example, a Covered Entity could use substituted compliance for internal risk management, trade acknowledgment and verification, internal supervision, and chief compliance officer requirements, but comply directly with Exchange Act portfolio reconciliation and dispute reporting, portfolio compression, trading relationship documentation, recordkeeping, reporting, notification, and securities count requirements.

[80] In the context of the UK EMIR counterparties condition in paragraph (a)(13) of the Order, a Covered Entity must choose (1) to apply substituted compliance pursuant to the Order—including compliance with paragraph (a)(13) as applicable—for a particular set of entity-level requirements with respect to all of its business that would be subject to the relevant UK EMIR-based requirement if the counterparty were the relevant type of counterparty, or (2) to comply directly with the Exchange Act with respect to such business. *See infra* note 106 and accompanying text.

[81] A third country investment firm regulated in the UK might be able to satisfy the definitions of ''Covered Entity'' in both this Order and the German Substituted Compliance Order, and thus may be eligible to apply substituted compliance under both orders. This Order defines Covered Entities to include both MiFID investment firms (*i.e.,* firms with a UK head office) and third country investment firms (*i.e.,* firms with a head office outside the UK). The German Substituted Compliance Order defines Covered Entities to include only investment firms and credit institutions ''authorized by BaFin to provide investment services or perform investment activities in the Federal Republic of Germany.'' *See* German Substituted Compliance Order, 85 FR at 85700. A non-EU firm (such as a UK firm) registered by the European Securities and Markets Authority (''ESMA'') to provide investment services and/or perform investment activities to certain counterparties in the EU pursuant to articles 46 through 48 of the Markets in Financial Instruments Regulation is not ''authorized by BaFin'' and thus does not satisfy the Covered Entity definition in the German Substituted Compliance Order. Accordingly, an investment firm or credit institution authorized by BaFin and regulated in the UK as a third country investment firm may, for example, be eligible for substituted compliance under both this Order and the German Substituted Compliance Order. If such a firm has security-based swap business that is not UK business, but is subject to the relevant German requirements under the German Substituted Compliance Order, it may choose to comply directly with the relevant Exchange Act requirements or to use substituted compliance pursuant to the terms of the German Substituted Compliance Order. If such a firm has security-based swap business that is both UK business and subject to the relevant German requirements under the German Substituted Compliance Order, it may choose to comply with the conditions to both orders or, alternatively, it may choose one order that it will comply with in respect of that business. For each set of entity-level Exchange Act requirements, such a firm must apply this choice to all such dually regulated security-based swap business. Such a firm must specify this choice in its notice to the Commission pursuant to para. (a)(16) of the Order. A firm's choice to comply with only one applicable substituted compliance order in respect of security-based swap business that is subject to the relevant foreign requirements listed in multiple substituted compliance orders will not affect the firm's ability to apply substituted compliance for Exchange Act entity-level requirements in respect of other, non–dually regulated security-based swap business under the other substituted compliance order(s).

[82] For example, a Covered Entity may use substituted compliance consistent with the Order for fair and balanced communications requirements in respect of communications with UK counterparties that are subject to the Exchange Act and comply directly with Exchange Act fair and balanced communications requirements in respect of U.S. person counterparties. A Covered Entity also may use substituted compliance consistent with the Order for any one or more sets of transaction-level Exchange Act requirements specified in the Order. *See supra* note 76 and accompanying text. For example, a Covered Entity could use substituted compliance for fair and balanced communications requirements, but comply directly with Exchange Act requirements related to disclosure of information regarding material risks and characteristics, disclosure of information regarding material incentives or conflicts of interest, ''know your counterparty,'' suitability, and daily mark disclosure.

[83] *See, e.g.,* Exchange Act section 15F(f); Exchange Act rule 18a–6(g).

necessary to facilitate the Commission's oversight under the Order.

c. Activities as UK ''Designated Investment Business''

One commenter recommended deleting paragraph (a)(4) of the proposed Order because ''MiFID business'' is a subset of ''designated investment business.'' [84] The commenter instead suggested adding FCA COBS 11 to the general condition in paragraph (a)(3) of the proposed Order, which is identical to paragraph (a)(4) except for the reference to ''designated investment business'' in paragraph (a)(4).

The only provision of FCA COBS 11 included in the Order is FCA COBS 11.7A.3R.[85] By its terms, FCA COBS 11.7A.3R applies to a firm's ''designated investment business.'' FCA COBS 11.7A.1R further states that FCA COBS 11.7A.3R applies, in relevant part, to a firm in relation to its ''MiFID or equivalent third country business.'' The condition as proposed thus accurately reflects the activities that FCA COBS describes as subject to FCA COBS 11.7A.3R. The Commission believes that deleting the reference to ''designated investment business'' would be inconsistent with the terms of the relevant provisions of FCA COBS 11. Moreover, the definitions of ''designated investment business'' and ''MiFID or equivalent third country business'' vary substantially. ''Designated investment business'' includes, among other things, dealing in investments as principal or agent, arranging deals in investments, making arrangements with a view to transactions in investments, managing investments, and advising on investments.[86] By contrast, ''MiFID or equivalent third country business'' includes, among other things, reception and transmission of orders in relation to one or more financial instruments, execution of orders on behalf of clients, dealing on own account, portfolio management, and the making of a personal recommendation.[87] Given the lack of overlap in terminology used in these two definitions, the Commission believes that deleting the reference to ''designated investment business'' could cause confusion among Covered Entities, while keeping the reference would not restrict a Covered Entity from being able to comply with the condition in respect of MiFID or equivalent third country business that is a subset of designated investment business. Accordingly the Commission has determined not to delete this paragraph.

d. Activities as UK ''MiFID Business''

One commenter recommended deleting paragraph (a)(5) of the proposed Order to reflect its recommendations to delete any FCA CASS provisions elsewhere in the Order as conditions to substituted compliance.[88] The commenter believes that the FCA CASS rules, which address client asset requirements, expand the scope of applicable Exchange Act requirements and are inappropriate as conditions to substituted compliance.[89] As discussed below in the relevant parts of this release,[90] the Commission has determined to retain the citations to FCA CASS as conditions to substituted compliance and, accordingly, has not deleted this paragraph.

e. Covered Entity as UK ''IFPRU Investment Firm''

One commenter recommended deleting paragraph (a)(11) of the proposed Order because the UK requirements listed in that paragraph do not apply to UK banks or UK designated investment firms and the commenter expects only ''banks and PRA-designated investment firms'' to apply substituted compliance pursuant to the Order.[91] These requirements apply to IFPRU investment firms—that is, certain investment firms regulated by the FCA but not the PRA—and are nearly identical to requirements that apply to UK banks and UK designated investment firms. For the same reason, the commenter also recommended deleting the references to firms regulated only by the FCA from the general conditions in paragraphs (a)(1) through (a)(3) and (a)(6) of the proposed Order and the UK requirements in paragraphs (b), (d), and (e) of the proposed Order that apply only to IFPRU investment firms.[92] The proposed Order would not require a Covered Entity that is a UK bank or UK designated investment firm to be subject to and comply with these requirements. Rather, in each place that the proposed Order refers to these requirements that are unique to IFPRU investment firms, the proposed Order would require the Covered Entity to be subject to and comply with either the provisions that apply to IFPRU investment firms (in which case paragraph (a)(11) of the proposed Order would require the Covered Entity to be an IFPRU investment firm) or analogous provisions of the FCA Handbook and PRA Rulebook that apply to UK banks and UK designated investment firms (in which case paragraph (a)(12) of the proposed Order would require the Covered Entity to be a UK bank or UK designated investment firm). Moreover, the FCA Application requested substituted compliance for all investment firms, and was not limited to the entities described by the commenter. Accordingly, the Commission is retaining the references to these requirements in paragraph (a)(11) and in paragraphs (b), (d), and (e) of the Order and the references to firms regulated only by the FCA in paragraphs (a)(1) through (a)(6) of the Order.

f. Counterparties as UK MiFID ''Clients''

A commenter requested that the Commission modify paragraph (a)(7) of the proposed Order to permit a Covered Entity to treat an agent, rather than the agent's principal, as the Covered Entity's client for purposes of the MiFID-based requirements listed in the Order.[93] The commenter stated that this modification would be consistent with the FCA's ''agent as client'' rule, which provides that a firm, if it is aware that a person with or for whom it is providing services is acting as agent for another person and satisfies certain other conditions, must treat the agent, and not the agent's principal, as the firm's client in respect of that business.[94] The firm may override the ''agent as client'' rule by agreeing in writing with the agent to treat the agent's principal as the firm's client instead.[95]

The proposed Order would require a Covered Entity to be ''subject to and comply with'' relevant MiFID-based requirements. The Commission proposed that requirement of the proposed Order to ensure that comparable MiFID-based requirements in practice would apply to a Covered Entity using substituted compliance. The condition in paragraph (a)(7) to the proposed Order would ensure that the Covered Entity's counterparty—*i.e.,* the entity to whom it owes its various duties under the Exchange Act—is the ''client'' to whom the Covered Entity owes its performance of the duties to which it is subject under the

[84] *See* SIFMA 5/3/2021 Letter Appendix A.

[85] *See* para. (d)(3)(ii) of the Order.

[86] *See* FCA Handbook Glossary, definition of ''designated investment business.''

[87] *See* FCA Handbook Glossary, definitions of ''MiFID or equivalent third country business,'' ''MiFID business,'' ''equivalent third country business,'' and ''investment services and/or activities.''

[88] *See* SIFMA 5/3/2021 Letter Appendix A.

[89] *See* SIFMA 5/3/2021 Letter Appendix A.

[90] *See infra* part VI.B.1.

[91] *See* SIFMA 5/3/2021 Letter Appendix A.

[92] *See* SIFMA 5/3/2021 Letter Appendix A parts (a), (b), (d), and (e).

[93] *See* SIFMA 5/3/2021 Letter at 4–6.

[94] *See* FCA COBS 2.4.3R.

[95] *See* FCA COBS 2.4.3R(2).

comparable MiFID-based requirements.[96] The Commission believes that, in the case of an agent acting on behalf of a principal, if the principal is the counterparty for purposes of the relevant Exchange Act requirement, then this condition should require the principal, as the counterparty, to be the ''client'' for purposes of the relevant MiFID-based requirements. If the Covered Entity instead treats the agent as the ''client,'' then the Covered Entity would not be ''subject to'' UK requirements that are comparable to Exchange Act requirements related to counterparties. Accordingly, the Commission is not amending the condition in paragraph (a)(7) to permit a Covered Entity to treat an agent, rather than the agent's principal, as its client with regard to the relevant MiFID-based requirements. In taking this position, the Commission does not prohibit Covered Entities from working with agents or others acting on behalf of a counterparty. Rather, the Covered Entity must ensure that, in working with the agent, it fulfills any duties owed to a ''client'' (or potential ''client'') in relation to the counterparty.[97]

g. UK EMIR Counterparties

A commenter requested that the Commission clarify that the condition in paragraph (a)(13) of the proposed Order would not require a Covered Entity to treat as financial counterparties or non-financial counterparties certain public sector counterparties, such as multilateral development banks, that are exempt from UK EMIR or counterparties that are not ''undertakings'' for purposes of UK EMIR's definitions of ''financial counterparty'' and ''non-financial counterparty.'' [98]

This condition addresses the fact that some of the UK EMIR-based requirements [99] are expressed to apply only to transactions between specified types of counterparties, such as transactions between financial counterparties and non-financial counterparties, between financial counterparties and non-financial counterparties above the clearing threshold, and/or between counterparties that are not excluded from the application of UK EMIR. The definitions of ''financial counterparty'' and ''non-financial counterparty'' are predicated on the counterparty being an ''undertaking'' established in the UK.[100] In addition, UK EMIR does not apply to transactions with certain excluded counterparties.[101] The condition is not based upon the concern that some industry participants may not be able to take advantage of substituted compliance, but, rather, the condition is intended to help ensure that the relevant UK EMIR-based requirements will apply in practice regardless of the counterparty's location or status as ''an undertaking.'' The condition provides that the Covered Entity must comply with the applicable condition of this Order as if the counterparty were the type of counterparty that would trigger the application of the relevant UK EMIR-based requirements. If the Covered Entity reasonably determines that its counterparty would be a financial counterparty[102] if not for the counterparty's location and/or lack of regulatory authorization in the UK, the condition further requires the Covered Entity to treat the counterparty as if the counterparty were a financial counterparty, rather than as another type of counterparty to which the relevant UK EMIR-based requirements may apply.[103] By requiring a Covered Entity to treat its counterparty as a type of counterparty that would trigger the application of the relevant UK EMIR-based requirements, the condition will require the Covered Entity to perform the relevant obligations pursuant to those UK EMIR-based requirements and thus to act in a way that is comparable to Exchange Act requirements. Accordingly, the Commission is retaining this condition to ensure that a Covered Entity can apply substituted compliance only when it treats its counterparty as a type of counterparty that will trigger the Covered Entity's performance of obligations pursuant to those UK EMIR-based requirements.[104] Because each UK EMIR-based requirement applies to different types of counterparties, the Commission is amending the condition to make clear that a Covered Entity must treat its

[96] Some provisions of the MiFID-based requirements cited in the condition, such as certain organizational requirements, do not pertain to counterparties or clients. In those cases, there is no ''relevant counterparty (or potential counterparty)'' for purposes of the condition, and the condition would have no effect.

[97] FCA COBS 2.4.4R permits firms to rely upon information about a client received from another UK-regulated firm. Under this provision, the other firm is legally responsible for the completeness and accuracy of any information about the client that the other firm receives from the first firm. The Commission believes that it is appropriate to permit a Covered Entity to rely on information about its client communicated by another UK-regulated firm on behalf of the client. Accordingly, the application of this provision would not cause the Covered Entity to be not ''subject to'' the relevant UK requirements listed in the Order, and thus would not impact the Covered Entity's ability to use substituted compliance in relation to those communications. On the other hand, FCA COBS 2.4.4R also provides that the other firm is legally responsible for the suitability of advice and recommendations provided to the client. The other firm, however, may not be a Covered Entity applying substituted compliance pursuant to the Order. Accordingly, the Commission believes that a Covered Entity relying on the suitability assessment of another firm pursuant to FCA COBS 2.4.4R is not ''subject to'' the relevant UK suitability requirements listed in the Order, and thus may not apply substituted compliance for those recommendations.

[98] *See* SIFMA 5/3/2021 Letter at 6 and Appendix A part (a) (recommending that the order text of paragraph (a)(13) of the Order require application of the condition ''if the counterparty to the Covered Entity is not a ''financial counterparty'' or ''non-financial counterparty'' as defined in UK EMIR articles 2(8) or 2(9) respectively, *solely because the counterparty is not established in the United Kingdom*'').

[99] *See, e.g.,* UK EMIR RTS article 12 (timely confirmation requirements for OTC derivatives contracts concluded between financial counterparties and non-financial counterparties).

[100] *See* UK EMIR article 2(8) (financial counterparties include specified UK financial firms and generally exclude non-UK entities); UK EMIR article 2(9) (non-financial counterparties include UK undertakings that are not financial counterparties and generally exclude natural persons, central counterparties, and non-UK entities).

[101] *See* UK EMIR articles 1(4) and 1(5) (UK EMIR does not apply to certain public sector and multilateral entities). Several of the multilateral development banks that the commenter mentioned are exempt from the definition of ''U.S. person'' in Exchange Act rule 3a71–3, 17 CFR 240.3a71–3, and, as a result, transactions between a foreign SBS Entity and one of those banks (without being arranged, negotiated, or executed by U.S. personnel) are not subject to most Exchange Act business conduct requirements. *See* UK EMIR article 1(5)(a) (exempting from UK EMIR multilateral development banks listed in UK CRR article 117); UK CRR article 117 (listed multilateral development banks include, among others, the International Bank for Reconstruction and Development, the Inter-American Development Bank, the Asian Development Bank, and the African Development Bank); Exchange Act rules 3a71–3(a)(4)(iii), (a)(7), (a)(8)(i), (a)(9) and (c); Exchange Act rules 3a67–10(a)(4), (a)(6) and (d)(1), 17 CFR 240.3a67–10(a)(4), (a)(6) and (d)(1).

[102] UK EMIR article 2(8) defines ''financial counterparty'' to encompass investment firms, credit institutions, insurers, and certain other types of businesses that have been authorized in accordance with UK law. Under UK EMIR, the distinction between financial counterparties and other types of counterparties such as non-financial counterparties is manifested, *inter alia,* in connection with confirmation timing standards. *See* UK EMIR RTS article 12.

[103] *See* para. (a)(13) of the Order. The condition will help clarify that the Covered Entity would be subject to the relevant UK EMIR-based requirements even if the counterparty is not an ''undertaking'' (such as by virtue of being a natural person), is not established in the EU (by virtue of being a U.S. person or otherwise being established outside the UK), or is excluded from the application of UK EMIR to its transactions (by virtue of being one of the public sector or multilateral entities identified in UK EMIR articles 1(4) and (5)).

[104] *See* para. (a)(13) of the Order. To correct a typographical error in the UK Substituted Compliance Notice and Proposed Order, in paragraph (a)(13) of the Order the Commission is changing the phrase ''paragraphs (b) through (e) of this Order'' to ''paragraphs (b) through (f) of this Order.'' This correction is consistent with the description of the proposed condition in the UK Substituted Compliance Notice and Proposed Order. *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18382.

counterparty as if the counterparty were the type of counterparty specified in the relevant UK EMIR-based requirement. The Commission also is amending the Order to clarify that the condition applies only if the relevant UK EMIR-based requirement applies solely to the Covered Entity's activities with specified types of counterparties. If the relevant UK EMIR-based requirement applies to a Covered Entity's activities without regard to the status of its counterparty,[105] the Covered Entity would not be required to treat its counterparty as any particular type of counterparty for purposes of that UK EMIR-based requirement.

As discussed in part III.B.2.b above, for any particular set of entity-level Exchange Act requirements, a Covered Entity must choose either (1) to apply substituted compliance pursuant to the Order with respect to all UK business, *i.e.,* security-based swap business that is subject to the relevant UK requirements listed in the Order and that can satisfy any general conditions related to those UK requirements; or (2) to comply directly with the Exchange Act with respect to all UK business. In the context of the UK EMIR counterparties condition in paragraph (a)(13), this scoping means that a Covered Entity's UK business includes security-based swap business that, but for the counterparty's failure to qualify as a type of counterparty specified in the relevant UK EMIR-based requirement, would be subject to the relevant UK EMIR-based requirement, and otherwise is subject to all other relevant UK requirements listed in the Order and can satisfy any other applicable general conditions.[106] Accordingly, a Covered Entity must choose (1) to apply substituted compliance pursuant to the Order—including compliance with paragraph (a)(13) as applicable—for a particular set of entity-level requirements with respect to all UK business, including its business that would be subject to the relevant UK EMIR-based requirement if the counterparty were the relevant type of counterparty; or (2) to comply directly with the Exchange Act with respect to all UK business.

H. Security-Based Swap Status Under UK EMIR

A commenter asked the Commission to amend the condition in paragraph (a)(14) of the proposed Order to permit a Covered Entity to apply substituted compliance for transactions cleared by a non-UK-regulated central counterparty.[107] As proposed, the condition helps to ensure that the relevant UK EMIR-based requirements will require the Covered Entity to treat its security-based swap in a manner comparable to Exchange Act requirements, while also clarifying that a Covered Entity still may apply substituted compliance in respect of transactions cleared by a UK-regulated central counterparty, even if the relevant UK EMIR-based requirements do not require the Covered Entity to take any action in respect of such a centrally cleared transaction. Many of the UK EMIR-based requirements cited in the Order relate to risk mitigation techniques for non-centrally cleared transactions and apply only to a non-centrally cleared OTC derivative,[108] consistent with analogous Exchange Act risk mitigation and margin requirements for non-centrally cleared security-based swaps.[109] However, transactions that have been cleared by any central counterparty, whether or not it is regulated by UK authorities, are exempt from these UK EMIR-based requirements, while only transactions that have been cleared by an SEC-registered or exempt clearing agency are exempt from their Exchange Act analogues. With respect to non-centrally cleared security-based swaps, the Commission believes that these UK requirements produce comparable outcomes to the analogous Exchange Act requirements, as both sets of requirements impose similar obligations on the Covered Entity. In addition, to the extent that these UK EMIR-based requirements do not require the Covered Entity to apply risk mitigation techniques to a security-based swap cleared by a UK-regulated central counterparty, the Commission also believes that these UK requirements produce comparable outcomes to the analogous Exchange Act requirements. The Commission reached this conclusion because neither set of requirements imposes risk mitigation techniques on transactions that have been cleared by central counterparties subject to regulation in the jurisdiction of the authority that supervises compliance with the risk mitigation requirements. However, to the extent that these UK EMIR-based requirements do not require the Covered Entity to apply risk mitigation techniques to the relevant security-based swap because it has been cleared by a non-UK-regulated central counterparty, the Commission does not believe that these UK requirements produce comparable outcomes to Exchange Act trade acknowledgment and verification, portfolio reconciliation and dispute reporting, portfolio compression, and trading relationship documentation requirements for non-centrally cleared security-based swaps. The Commission reached this conclusion because these Exchange Act requirements exempt centrally cleared security-based swaps only if they have been cleared by an SEC-registered clearing agency (or, in the case of portfolio reconciliation and dispute reporting, portfolio compression, and trading relationship documentation requirements, a clearing agency that the Commission has exempted from registration). Security-based swaps that have been cleared by a central counterparty that is not SEC-registered or exempt or UK-regulated are subject to those Exchange Act requirements, but are not subject to the UK EMIR-based risk mitigation requirements. Accordingly, the Commission is issuing the condition as proposed to require that the relevant security-based swap is either (a) an OTC derivative or OTC derivative contract that has not been cleared by any central counterparty and is otherwise subject to the relevant UK EMIR-based requirements or (b) cleared by a UK-regulated central counterparty.[110]

As an alternative to its suggested amendments to the condition, the commenter asked the Commission to permit the Covered Entity to comply directly with the Exchange Act (or with another applicable substituted compliance order) with respect to transactions cleared by a non-UK-

[105] *See, e.g.,* UK EMIR articles 39(4) and (5).

[106] A Covered Entity's business that is not subject to other non-UK EMIR-based requirements listed in the Order or that does not satisfy any other applicable general condition would not form part of a Covered Entity's UK business for which the Covered Entity must make a single choice between using substituted compliance or complying directly with the Exchange Act. For example, for purposes of its choice to apply substituted compliance or comply directly with Exchange Act internal risk management requirements, a Covered Entity need not treat as UK business a transaction that is not subject to FCA SYSC 4.1.1R(1) or that cannot satisfy the general conditions in paragraphs (a)(1) and (a)(10) of the Order, even if the sole reason the transaction is not subject to UK EMIR Margin RTS article 2 is that the counterparty is not the type of counterparty to which that requirement applies.

[107] *See* SIFMA 5/3/2021 Letter at 6–7.

[108] *See, e.g.,* UK EMIR article 11.

[109] *See, e.g.,* Exchange Act rules 15Fi–2, 17 CFR 240.15Fi–2 through 15Fi–4, 17 CFR 240.15Fi–4; Exchange Act rule 18a–3, 17 CFR 240.18a–3.

[110] *See* para. (a)(14) of the Order. To correct a typographical error in the UK Substituted Compliance Notice and Proposed Order, in paragraph (a)(14) of the Order the Commission is changing the phrase ''paragraphs (b) through (e) of this Order'' to ''paragraphs (b) through (f) of this Order.'' This correction is consistent with the description of the proposed condition in the UK Substituted Compliance Notice and Proposed Order. *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18382.

regulated central counterparty, and to do so without affecting the Covered Entity's ability to apply substituted compliance for entity-level requirements with respect to other security-based swap business that does satisfy the condition.[111] Consistent with the discussion of the scope of substituted compliance for entity-level requirements in part III.B.2.b above, for entity-level Exchange Act requirements, a Covered Entity must choose either (1) to apply substituted compliance pursuant to the Order with respect to all UK business (that is, security-based swap business that is both subject to the relevant UK requirements listed in the Order and that can satisfy any general conditions related to those UK requirements, including paragraph (a)(14)); or (2) to comply directly with the Exchange Act with respect to all UK business. A transaction cleared by a non-UK-regulated central counterparty does not satisfy the condition in paragraph (a)(14) of the Order. As a result, paragraph (a)(14) would not permit a Covered Entity to use substituted compliance for any Exchange Act requirements that apply to that transaction if the relevant conditions in parts (b) through (f) of the Order include a requirement for the Covered Entity to be subject to and comply with provisions of UK EMIR, UK EMIR RTS, UK EMIR Margin RTS, and/or other UK requirements adopted pursuant to those provisions. Instead, a Covered Entity must either comply directly with the Exchange Act for such a transaction or comply with the terms of another applicable substituted compliance order that the transaction is able to satisfy.[112] Such a transaction would not be included in the UK business for which a Covered Entity must elect a single choice—use substituted compliance under the Order or comply directly with the Exchange Act—when complying with entity-level Exchange Act requirements.

The commenter also requested that the Commission revise the condition's description of UK-regulated central counterparties to clarify that it includes UK-regulated third country central counterparties, which may have a domicile outside the UK and thus may not be viewed as ''recognized to clear derivatives contracts *in* the UK.'' [113] Similarly, the commenter asked the Commission to further revise the description to encompass the UK's temporary recognition regime for third country central counterparties implemented as a consequence of the UK's exit from the European Union.[114] The Commission intends the condition's description of UK-regulated central counterparties to include third country central counterparties that relevant UK authorities allow to provide clearing services to UK clearing members or trading venues.[115] These central counterparties include those ''taken to be'' recognized pursuant to the UK's temporary recognition regime for third country central counterparties.[116] Accordingly, the Commission is amending the condition's description of UK-regulated central counterparties so that it describes ''a central counterparty that is authorized, recognized, or taken to be recognized by a relevant UK authority to provide clearing services to clearing members or trading venues established in the UK.'' [117]

Finally, the Commission is amending the condition to clarify that the condition applies only if the relevant UK EMIR-based requirement applies to OTC derivatives that have not been cleared by a central counterparty, as some provisions of UK EMIR cited in the Order, such as UK EMIR articles 39(4) and (5), are not limited in their application to non-centrally cleared OTC derivatives. Consistent with the condition in paragraph (a)(13) of the Order, the Commission also is adding references to UK EMIR RTS and UK EMIR Margin RTS.

i. Memorandum of Understanding

As proposed, the Commission would need to have a supervisory and enforcement memorandum of understanding and/or other arrangement with the FCA and the PRA addressing cooperation with respect to the Order at the time the Covered Entity makes use of substituted compliance.[118] This condition has been modified from the proposed Order to reflect that the executed version of the memorandum of understanding is between the Commission, on the one hand, and the FCA and the Bank of England (including in its capacity as the PRA), on the other hand.

j. Notice of Reliance on Substituted Compliance

Commenters did not address the requirement in paragraph (a)(16) of the proposed Order for the Covered Entity to notify the Commission in writing of its intent to rely on substituted compliance, and the Commission is adopting this requirement as proposed.[119]

[111] *See* SIFMA 5/3/2021 Letter at 7.

[112] *See supra* note 80.

[113] *See* SIFMA 5/3/2021 Letter at 7.

[114] *See* SIFMA 5/3/2021 Letter at 7.

[115] *See* UK EMIR article 25(1) (a third country central counterparty may provide clearing services to UK clearing members or trading venues only if it is recognized by the Bank of England); *see also* The Over the Counter Derivatives, Central Counterparties and Trade Repositories (Amendment, etc., and Transitional Provision) (EU Exit) Regulations 2020 (2020/646), regulation 20(2).

[116] *See* The Central Counterparties (Amendment, etc., and Transitional Provision) (EU Exit) Regulations 2018 (2018/1184), part 6.

[117] *See* para. (a)(14)(ii) of the Order. The Commission also is amending the condition so that it applies to conditions of the Order that require the application of, and the Covered Entity's compliance with, UK EMIR, UK EMIR RTS, UK EMIR Margin RTS, and/or other UK requirements adopted pursuant to those requirements.

[118] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18412.

[119] *See* para. (a)(16) of the Order. If the Covered Entity intends to rely on all the substituted compliance determinations in a given paragraph of the Order, it can cite that paragraph in the notice. For example, if the Covered Entity intends to rely on the capital and margin determinations in paragraph (c) of the Order, it can indicate in the notice that it is relying on the determinations in paragraph (c). However, if the Covered Entity intends to rely on the margin determination but not the capital determination, it will need to indicate in the notice that it is relying on paragraph (c)(2) of the Order (the margin determination). In this case, paragraph (c)(1) of the Order (the capital determination) will be excluded from the notice and the Covered Entity will need to comply with the Exchange Act capital requirements. Further, as discussed below in part VIII.B.1, the recordkeeping and reporting determinations in the Order have been structured to provide Covered Entities with a high level of flexibility in selecting specific requirements within those rules for which they want to rely on substituted compliance. For example, paragraph (f)(1)(i) of the Order sets forth the Commission's substituted compliance determinations with respect to the requirements of Exchange Act rule 18a–5, 17 CFR 240.18a–5. These determinations are set forth in paragraphs (f)(1)(i)(A) through (O) of the Order. If a Covered Entity intends to rely on some but not all of the determinations, it will need to identify in the notice the specific determinations in this paragraph it intends to rely on (*e.g.,* paragraphs (f)(1)(i)(A), (B), (C), (D), (G), (H), (I), and (O)). For any determinations excluded from the notice, the Covered Entity will need to comply with the Exchange Act rule 18a–5 requirement. Finally, a Covered Entity is able to apply substituted compliance at the transaction level (rather than the entity level) for certain counterparty protection requirements and the recordkeeping requirements that are linked to them. In this case, the notice will need to indicate the class of transactions (*e.g.,* transactions with UK counterparties) for which the Covered Entity is applying substituted compliance with respect to the Exchange Act counterparty protection requirements and linked recordkeeping requirements. Similarly, as discussed above, a Covered Entity is able to apply substituted compliance for entity-level Exchange Act requirements to all of its security-based swap business that is eligible for substituted compliance under the Order, and may either comply directly with the Exchange Act or apply substituted compliance under another applicable order for its security-based swap business that is not eligible for substituted compliance under the Order. In this case, the notice will need to indicate the scope of security-based swap business (*e.g.,* security-based swap business carried on from an establishment in the UK) for which the Covered Entity is applying substituted compliance with respect to the relevant Exchange Act entity-level requirements. A Covered

Continued

k. Notification Requirements Related to Changes in Capital

In response to the French Substituted Compliance Notice and Proposed Order, a commenter requested that the Commission make more granular substituted compliance determinations with respect to the Exchange Act recordkeeping requirements.[120] The commenter stated that for ''operational reasons'' a Covered Entity may ''prefer to comply directly with certain Exchange Act requirements (*i.e.,* not to rely on substituted compliance with those requirements).'' [121] The Commission took this approach in the proposed Order with respect to the Exchange Act recordkeeping, reporting, and notification requirements.[122] As part of this approach, the Commission also conditioned substituted compliance with certain of the discrete recordkeeping, reporting, and notification requirements on the Covered Entity applying substituted compliance with respect to the substantive Exchange Act requirement to which they were linked.[123] This linked condition was designed to ensure that a Covered Entity consistently applies substituted compliance with respect to the substantive Exchange Act requirement and the Exchange Act recordkeeping, reporting, or notification requirement that complements the substantive requirement.

On further consideration and in light of the more granular approach requested by the commenter, the Commission believes it necessary to do the reverse with respect to certain substantive financial responsibility requirements: Condition substituted compliance with respect to the substantive requirement on the Covered Entity applying substituted compliance with respect to the linked recordkeeping, reporting, or notification requirement. The Exchange Act financial responsibility requirements addressed in this Order (capital, margin, recordkeeping, reporting, notification, and securities count requirements) are highly integrated. Therefore, implementing the reverse conditional link is designed to ensure that the granular approach requested by the commenter results in comparable regulatory outcomes in terms of obligations to make and preserve records, and to submit reports and notifications to the Commission concerning the Covered Entity's compliance with the financial responsibility rules. It also is designed to provide clarity as to the obligations of a Covered Entity under this Order when using the granular approach to the Exchange Act recordkeeping, reporting, and notification requirements linked to the financial responsibility rules.

For example, because of the granular approach, a Covered Entity could elect to apply substituted compliance with respect to a substantive Exchange Act requirement such as the capital requirements of Exchange Act rule 18a–1 but elect not to apply substituted compliance with respect to a linked requirement under Exchange Act rule 18a–8 to provide the Commission notice of a capital deficiency under Exchange Act rule 18a–1. In this scenario, the Covered Entity would not be subject to the condition for applying substituted compliance with respect to Exchange Act rule 18a–8; namely, that the firm provide the Commission copies of notifications relating to UK capital requirements required under UK law. Consequently, as discussed below in this section and other sections of this release, the Commission is conditioning substituted compliance with respect to certain substantive Exchange Act requirements on the Covered Entity applying substituted compliance with respect to linked recordkeeping, reporting, or notification requirements.

Exchange Act Rule 18a–8(c)

Exchange Act rule 18a–8(c) generally requires every prudentially regulated security-based swap dealer that files a notice of adjustment of its reported capital category with the Federal Reserve Board, the Office of the Comptroller of the Currency, or the Federal Deposit Insurance Corporation to give notice of this fact that same day by transmitting a copy to the Commission of the notice of adjustment of reported capital category in accordance with Exchange Act rule 18a–8(h).[124] Exchange Act rule 18a–8(h) sets forth the manner in which every notice or report required to be given or transmitted pursuant to Exchange Act rule 18a–8 must be made.[125] While Exchange Act rule 18a–8(c) is not linked to a substantive Exchange Act requirement, it is linked to substantive capital requirements applicable to prudentially regulated SBS Entities in the U.S. (*i.e.,* capital requirements of the Federal Reserve Board, the Office of the Comptroller of the Currency, or the Federal Deposit Insurance Corporation). Therefore, to implement the granular approach requested by the commenter, the Commission is adding a general condition that Covered Entities with a prudential regulator relying on the final Order for substituted compliance must apply substituted compliance with respect to the requirements of Exchange Act rule 18a–8(c) and the requirements of Exchange Act rule 18a–8(h) as applied to Exchange Act rule (c).[126]

In its application, the FCA cited several UK provisions as providing similar outcomes to the notification requirements of Exchange Act rule 18a–8.[127] This general condition is necessary

Entity would modify its reliance on the positive substituted compliance determinations in the Order, and thereby trigger the requirement to update its notice, if it adds or subtracts determinations for which it is applying substituted compliance or completely discontinues its reliance on the Order.

[120] *See* Letter from Kyle Brandon, Managing Director, Head of Derivative Policy, SIFMA (Jan. 25, 2021) (''SIFMA 1/25/2021 Letter'') at 8.

[121] SIFMA 1/25/2021 Letter at 8.

[122] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR 18394–403, 18415–420.

[123] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR 18394–403, 18415–420.

[124] *See* 17 CFR 240.18a–8(c).

[125] *See* 17 CFR 240.18a–8(h).

[126] Better Markets Letter at 2–3.

[127] These UK provisions include: (1) FCA PRIN 2.1.1R (Principle 11) and PRA Fundamental Rule 7 requiring firms to deal with regulators in an open and cooperative way, and to disclose to regulators anything relating to the firm of which the regulator would reasonably expect notice; (2) Supervision Sourcebook of the FCA Handbook (''FCA SUP'') 15.3.1R and PRA Notification Rule 2.1, which require immediate notification if a firm becomes aware that certain events have occurred or may occur in the foreseeable future, including the failure of the firm to satisfy certain threshold conditions, any matter which could have a significant adverse impact on the firm's reputation or that could affect the firm's ability to continue to provide adequate services to its customers or result in serious detriment to its customers, or any matter which could result in serious financial consequences to the UK financial system or other firms; (3) FCA SUP 15.3.11R and PRA Notification Rule 2.4, which generally require, among other things, notification of a significant breach of a rule or certain specified provisions or regulations, or the bringing of a prosecution related to certain offenses; (4) FCA SUP 15.3.15R and PRA Notification Rule 2.6, which require a firm to provide immediate notification in the event that civil proceedings or other specified actions are brought against the firm, if disciplinary measures or sanctions are imposed on the firm, if the firm is prosecuted for, or convicted of, any offense involving fraud, or it is removed as a trustee of an occupational pension scheme by a court order; (5) FCA SUP 15.17R and PRA Notification Rule 2.8, which require a firm to provide notification in the event that, among other things, the firm becomes aware that an employee, or another person whether or not employed by the firm, may have committed a fraud against a customer, or the firm identifies irregularities in its accounting or other records; (6) FCA SUP 15.3.21R and PRA Notification Rule 2.9, which require a firm to provide immediate notification upon the calling of a meeting to consider a resolution, or the presentation of a petition, for winding up the firm, an application to dissolve the firm, or other similar matters; (7) FCA CASS 6.6.57R and 7.15.33R, which require, among other things, notification if a firm's internal records and accounts related to client assets and money are materially out of date, inaccurate, or invalid, the firm fails or is unable to respond to shortfalls as required, or the firm fails or is unable to conduct an internal asset reconciliation, external custody reconciliation, or internal and external client money reconciliations; and (8) FCA SYSC 18.6.1R and PRA Organisational Requirements 2A.1(2), 2A.2, and 2A.3 through 2A.6, which require firms

in order to clarify that a prudentially regulated Covered Entity must provide the Commission with copies of any notifications regarding changes in the Covered Entity's capital situation required by UK law. In particular, a prudentially regulated Covered Entity could elect not to apply substituted compliance with respect to Exchange Act rule 18a–8(c). However, because the Covered Entity is not required to provide any notifications to the Federal Reserve Board, the Office of the Comptroller of the Currency, or the Federal Deposit Insurance Corporation, ''compliance'' with the provisions of Exchange Act rule 18a–8(c) raises a question as to the Covered Entity's obligations under this Order to provide the Commission with notification of changes in capital.

Moreover, a commenter stated that foreign financial services firms were among the entities that used emergency lending facilities in the U.S. along with other U.S. measures to address the 2008 financial crisis.[128] The Commission adopted Exchange Act rule 18a–8(c) to require SBS Entities with a prudential regulator to give notice to the Commission when filing an adjustment of reported capital category because such notices may indicate that the entity is in or is approaching financial difficulty.[129] The Commission has a regulatory interest in being notified of changes in the capital of a prudentially regulated Covered Entity, as it could signal the firm is in or approaching financial difficulty and presents a risk to U.S. security-based swap markets and participants. For the foregoing reasons, the Commission is conditioning applying substituted compliance pursuant to the Order on the general condition that a prudentially regulated Covered Entity apply substituted compliance with respect to Exchange Act rule 18a–8(c) and the requirements of Exchange Act rule 18a–8(h) as applied to Exchange Act rule 18a–8(c).

IV. Substituted Compliance for Risk Control Requirements

A. Proposed Approach

The FCA Application in part requested substituted compliance in connection with risk control requirements relating to:

- Internal risk management—Internal risk management system requirements that address the obligation of registered entities to follow policies and procedures reasonably designed to help manage the risks associated with their business activities.
- Trade acknowledgment and verification—Trade acknowledgment and verification requirements intended to help avoid legal and operational risks by requiring definitive written records of transactions and procedures to avoid disagreements regarding the meaning of transaction terms.
- Portfolio reconciliation and dispute reporting—Portfolio reconciliation and dispute reporting provisions that require that counterparties engage in portfolio reconciliation and resolve discrepancies in connection with uncleared security-based swaps, and to provide prompt notification to the Commission and applicable prudential regulators regarding certain valuation disputes.
- Portfolio compression—Portfolio compression provisions that require that SBS Entities have procedures addressing bilateral offset, bilateral compression, and multilateral compression in connection with uncleared security-based swaps.
- Trading relationship documentation—Trading relationship documentation provisions that require SBS Entities to have procedures to execute written security-based swap trading relationship documentation with their counterparties prior to, or contemporaneously with, executing certain security-based swaps.[130]

Taken as a whole, these risk control requirements help to promote market stability by mandating that registered entities follow practices that are appropriate to manage the market, counterparty, operational, and legal risks associated with their security-based swap businesses.

In proposing to provide conditional substituted compliance in connection with this part of the FCA Application, the Commission preliminarily concluded that the relevant UK requirements in general would help to produce regulatory outcomes that are comparable to those associated with Exchange Act risk control requirements, by subjecting Covered Entities to risk mitigation and documentation practices that are appropriate to the risks associated with their security-based swap businesses.[131] Substituted compliance under the proposed Order was to be conditioned in part on Covered Entities being subject to and complying with the specified UK provisions that in the aggregate help to produce outcomes that are comparable to those associated with the risk control requirements under the Exchange Act.[132]

Substituted compliance under the proposed Order further would be subject to certain additional conditions to help ensure the comparability of outcomes. First, substituted compliance for Exchange Act trading relationship documentation requirements would not extend to certain disclosures regarding legal and bankruptcy status.[133] Second, substituted compliance for portfolio reconciliation and dispute reporting requirements would be conditioned on the Covered Entity having to provide the Commission with reports regarding disputes between counterparties on the same basis as the Covered Entity provides those reports to the FCA pursuant to UK law.[134]

to have arrangements or procedures in place for employees to report potential or actual breaches or reportable concerns.

[128] Better Markets Letter at 2.

[129] *See* Exchange Act Release No. 71958 (September 19, 2019), 84 FR 68550, 68589–90 (Dec. 16, 2019) (''Recordkeeping and Reporting Adopting Release'') (citing Exchange Act Release No. 71958 (Aug. 17, 2014) 79 FR 25193 (May 2, 2014) at 25249).

[130] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18383.

[131] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18383.

[132] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18383 and n.61. Each of the comparable UK requirements listed in the proposed Order applies to a uniquely defined set of UK-authorized firms. *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18384–85 and n.70. To assist UK firms in determining whether they are subject to these requirements, the Commission preliminarily determined that any Covered Entity that is an ''IFPRU investment firm,'' ''UK bank'' or ''UK designated investment firm,'' each as defined for purposes of UK law, would be subject to all of the required UK requirements related to internal risk management requirements and thus eligible to apply substituted compliance for internal risk management requirements. The Commission also preliminarily determined that a Covered Entity that is a ''financial counterparty'' would be subject to the required UK requirements related to trade acknowledgment and verification, portfolio reconciliation and dispute reporting, portfolio compression, and trading relationship documentation and thus eligible to apply substituted compliance in these areas. *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18384–85.

[133] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18383. The trading relationship documentation provisions of rule 15Fi–5(b)(5), 17 CFR 240.15Fi–5(b)(5), require certain disclosures regarding the status of the SBS Entity or its counterparty as an insured depository institution or financial counterparty, and regarding the possible application of the insolvency regime set forth under Title II of the Dodd-Frank Act or the Federal Deposit Insurance Act. Documentation requirements under applicable UK law would not be expected to address the disclosure of information related to insolvency procedures under U.S. law.

[134] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18383. Under the Exchange Act requirement, SBS Entities must promptly report, to the Commission, valuation disputes in excess of $20 million that have been outstanding for three or five business days (depending on counterparty types). UK requirements provide that firms must report at least monthly, to the FCA, disputes between counterparties in excess of €15 million and outstanding for at least 15 business days.

B. Commenter Views and Final Provisions

After considering commenters' recommendations regarding the risk control requirements, the Commission is making positive substituted compliance determinations in connection with internal risk management, trade acknowledgment and verification, portfolio reconciliation and dispute reporting, portfolio compression, and trading relationship documentation requirements. As discussed below, the final Order has been changed from the proposed Order in certain respects in response to comments.[135]

One commenter expressed general support for the proposed approach toward substituted compliance for the risk control provisions.[136] Another commenter stated that UK requirements are not sufficiently comparable to Exchange Act requirements.[137] The Commission continues to conclude that, taken as a whole, applicable requirements under UK law subject Covered Entities to risk mitigation and documentation practices that are appropriate to the risks associated with their security-based swap businesses, and thus help to produce regulatory outcomes that are comparable to the outcomes associated with the relevant risk control requirements under the Exchange Act. Although the Commission recognizes that there are differences between the approaches taken by the relevant risk control requirements under the Exchange Act and relevant UK requirements, the Commission continues to believe that those differences on balance should not preclude substituted compliance for these requirements, as the relevant UK requirements taken as a whole help to produce comparable regulatory outcomes.

To help ensure the comparability of outcomes, substituted compliance for risk control requirements is subject to certain conditions. Substituted compliance for internal risk management, trade acknowledgment and verification, portfolio reconciliation and dispute reporting, portfolio compression, and trading relationship documentation requirements is conditioned on the Covered Entity being subject to, and complying with, relevant UK requirements.[138] In addition, consistent with the proposed Order, substituted compliance for portfolio reconciliation and dispute reporting requirements is conditioned on the Covered Entity providing the Commission with reports regarding disputes between counterparties on the same basis as the Covered Entity provides those reports to the FCA pursuant to UK law.[139] Finally, consistent with the proposed Order, substituted compliance for trading relationship documentation does not extend to disclosures regarding legal and bankruptcy status that are required by Exchange Act rule 15Fi–5(b)(5) when the counterparty is a U.S. person.[140] A Covered Entity that is unable to comply with an applicable condition—and thus is not eligible to use substituted compliance for the particular set of Exchange Act risk control requirements related to that condition—nevertheless may use substituted compliance for another set of Exchange Act requirements addressed in the Order if it complies with the conditions to the relevant parts of the Order.

Under the Order, substituted compliance for risk control requirements (relating to internal risk management, trade acknowledgment and verification, portfolio reconciliation and dispute reporting, portfolio compression, and trading relationship documentation) is not subject to a condition that the Covered Entity apply substituted compliance for related recordkeeping requirements in Exchange Act rules 18a–5 and 18a–6. A Covered Entity that applies substituted compliance for one or more risk control requirements, but does not apply substituted compliance for the related recordkeeping requirements in Exchange Act rules 18a–5 and 18a–6, will remain subject to the relevant provisions of Exchange Act rules 18a–5 and 18a–6. Those rules require the Covered Entity to make and preserve records of its compliance with Exchange Act risk control requirements and of its security-based swap activities required or governed by those requirements. A Covered Entity that applies substituted compliance for a risk control requirement, but complies directly with related recordkeeping requirements in rules 18a–5 and 18a–6, therefore must make and preserve records of its compliance with the relevant conditions to the Order and of its security-based swap activities required or governed by those conditions and/or referenced in the relevant parts of rules 18a–5 and 18a–6.

The Commission details below its consideration of comments on the proposed Order.

1. Internal Risk Management

Exchange Act section 15F(j)(2) requires a registered SBS Entity to establish robust and professional risk

[135] *See* para. (b) of the Order.

[136] *See* SIFMA 5/3/2021 Letter at 9. The commenter also requested that the Commission not require a Covered Entity to be subject to and comply with some of the UK risk control requirements listed in the proposed Order. *See* SIFMA 5/3/2021 Letter at 9 and Appendix A part (b). The Commission addresses those requests in the relevant sections of this part IV below.

[137] *See* Better Markets Letter at 2. The commenter also stated that, if the Commission nevertheless makes a positive substituted compliance determination, it must at a minimum ensure that the conditions in the proposed Order ''are applied with full force and without exceptions or dilution.'' The Commission addresses that comment in the relevant sections of this part IV below.

[138] *See* paras. (b)(1) through (b)(5) of the Order.

[139] *See* paras. (b)(3)(ii) of the Order. This condition promotes comparability with the Exchange Act rule requiring reports to the Commission regarding significant valuation disputes, while leveraging UK reporting provisions to avoid the need for Covered Entities to create additional reporting frameworks. When it proposed the condition to report valuation disputes, the Commission recognized that valuation inaccuracies may lead to uncollateralized credit exposure and the potential for loss in the event of default. *See* Exchange Act Release No. 84861 (Dec. 19, 2018), 84 FR 4614, 4621 (Feb. 15, 2019). It thus is important that the Commission be informed regarding valuation disputes affecting SBS Entities. The principal difference between the Exchange Act and UK valuation dispute reporting requirements concerns the timing of notices. Exchange Act rule 15Fi–3 requires SBS Entities to report promptly to the Commission valuation disputes in excess of $20 million that have been outstanding for three or five business days (depending on the counterparty type). UK EMIR RTS article 15(2) requires financial counterparties to report to the FCA at least monthly any disputes between counterparties in excess of €15 million and outstanding for at least 15 business days. The Commission is mindful that the UK provision does not provide for notice as quickly as rule 15Fi–3, but in the Commission's view on balance this difference would not be inconsistent with the conclusion that the two sets of requirements, taken as a whole, promote comparable regulatory outcomes.

[140] *See* para. (b)(5) of the Order. The Exchange Act rule 15Fi-5 disclosures address information regarding (1) the status of the SBS Entity or its counterparty as an insured depository institution or financial counterparty and (2) the possibility that in certain circumstances the SBS Entity or its counterparty may be subject to the insolvency regime set forth in Title II of the Dodd-Frank Wall Street Reform and Consumer Protection Act or the Federal Deposit Insurance Act, which may affect rights to terminate, liquidate, or net security-based swaps. *See* Exchange Act Release No. 87782 (Dec. 18, 2019), 85 FR 6359, 6374 (Feb. 4, 2020) (''Risk Mitigation Adopting Release''). Documentation requirements under applicable UK law do not address the disclosure of information related to insolvency procedures under U.S. law. However, the absence of such disclosures would not appear to preclude a comparable regulatory outcome when the counterparty is not a U.S. person, as the insolvency-related consequences that are the subject of the disclosure would not apply to non-U.S. counterparties in most cases. Moreover, UK EMIR Margin RTS article 2 requires counterparties to establish, apply, and document risk management procedures providing for or specifying the terms of agreements entered into by the counterparties, including applicable governing law for non–centrally cleared derivatives. When counterparties enter into a netting or collateral exchange agreement, they also must perform an independent legal review of the enforceability of those agreements.

management systems adequate for managing its day-to-day business. In addition, Exchange Act rule 15Fh–3(h)(2)(iii)(I) [141] requires an SBS Entity to establish and maintain a system to supervise, and to diligently supervise, its business and the activities of its associated persons. This system of internal supervision must include, in relevant part, the establishment, maintenance, and enforcement of written policies and procedures reasonably designed, taking into consideration the nature of the SBS Entity's business, to comply with its duty under Exchange Act section 15F(j)(2) to establish an internal risk management system.

The Commission continues to believe that UK internal risk management requirements promote regulatory outcomes comparable to Exchange Act requirements, and is making a positive substituted compliance determination for internal risk management requirements that is consistent with the proposed Order except for the addition of certain risk management requirements. A commenter requested that the Commission not require a Covered Entity to be subject to and comply with certain of the UK requirements specified in the proposed Order.[142] By contrast, another commenter stated that, if the Commission makes a positive substituted compliance determination, it must at a minimum ensure that the conditions in the proposed Order ''are applied with full force and without exceptions or dilution.'' [143] The Commission details below its consideration of comments received.

A commenter stated that the Commission should delete from the Order the provisions of FCA IFPRU, FCA BIPRU, and FCA SYSC 19A listed in paragraphs (b)(1)(i) and (b)(1)(iv) of the proposed Order. These provisions apply only to IFPRU investment firms, and the commenter stated that it expects only ''banks and PRA-designated investment firms'' will register as SBS Entities.[144] For the reasons described in part III.B.2.e above, the Commission is retaining the references to these provisions.

Similarly, the commenter stated that the Commission should delete from the Order the provisions of FSMA and FCA COND listed in paragraph (b)(1)(v) of the proposed Order that apply to firms regulated only by the FCA, rather than to firms dually regulated by both the FCA and the PRA.[145] The commenter again stated that it expects only dually regulated ''banks and PRA-designated investment firms'' will register as SBS Entities.[146] The proposed Order would not require a Covered Entity that is a dually regulated firm to be subject to and comply with these provisions. Rather, paragraph (b)(1)(v) of the proposed Order would require the Covered Entity to be subject to and comply with either the provisions of FSMA and FCA COND that apply to solo-regulated firms or analogous provisions that apply to dually regulated firms. Accordingly, the Commission is retaining the references to these provisions.

The commenter also recommended that the Commission delete from the Order the following provisions because they do not correspond to and go beyond Exchange Act internal risk management requirements: [147]

- PRA Internal Capital Adequacy Assessment Rules 4.1 through 4.4, which implement CRD article 79, address a Covered Entity's management of credit and counterparty risk. PRA Internal Capital Adequacy Assessment Rule 5.1, which implements CRD article 80, addresses a Covered Entity's management of residual risk. PRA Internal Capital Adequacy Assessment Rule 6.1, which implements CRD article 81, addresses a Covered Entity's management of concentration risk. PRA Internal Capital Adequacy Assessment Rules 7.1 and 7.2, which implement CRD article 82, address a Covered Entity's management of securitization risk. PRA Internal Capital Adequacy Assessment Rules 8.1 through 8.5, which implement CRD article 83, address a Covered Entity's management of market risk. PRA Internal Capital Adequacy Assessment Rule 9.1, which implements CRD article 84, addresses a Covered Entity's management of interest rate risk. PRA Internal Capital Adequacy Assessment Rules 10.1 and 10.2, which implement CRD article 85, address a Covered Entity's management of operational risk. PRA Internal Liquidity Adequacy Assessment Rules 3.1 through 3.3, 4.1, 7.2, 8.1, 9.2, 11.1, 11.2, 11.4, 12.1, 12.3, and 12.4, which implement CRD article 86, address a Covered Entity's management of liquidity risk and funding risk. PRA Internal Capital Adequacy Assessment Rules 11.1 through 11.3, which implement CRD article 87, address a Covered Entity's management of risk from excessive leverage.
- FCA SYSC 4.1.1R, which implements a portion of CRD article 74(1), requires a Covered Entity to have robust governance arrangements, including effective processes to identify, manage, monitor, and report the risks it is or might be exposed to. FCA SYSC 4.1.2R and PRA General Organisational Requirement Rule 2.2, which implement CRD article 74(2), requires these arrangements and processes to be comprehensive and proportionate to the nature, scale, and complexity of the risks of the Covered Entity's business and activities. FCA SYSC 7.1.4R, 7.1.17R, 7.1.18R, 7.1.18BR, 7.1.19R, 7.1.20R, 7.1.21R, and 7.1.22R and PRA Risk Control Rules 2.3, 2.7, and 3.1 through 3.5, which implement CRD article 76, address the Covered Entity's internal governance structures for risk management.
- FCA SYSC 19D.2.1R and PRA Remuneration Rule 6.2 require a Covered Entity to establish and maintain a remuneration policy, practices, and procedures that are consistent with and that promote sound and effective risk management.[148]
- FSMA schedule 6 part 3C and FCA COND 2.4.1C, which address issues similar to MiFID articles 16(4) and (5), require the Covered Entity's non-financial resources to be appropriate in relation to its regulated activities, taking into account factors such as the nature and scale of the business, the risks to the continuity of the Covered Entity's services, the Covered Entity's membership in a group or any effect that membership may have, the skills and experience of those managing the Covered Entity's affairs, and whether the Covered Entity's non-financial resources are sufficient to enable it to comply with applicable requirements of the FCA. FSMA schedule 6 part 5D, which also addresses issues similar to MiFID articles 16(4) and (5), requires the Covered Entity's business to be conducted in a prudent manner, which requires the Covered Entity to have appropriate financial and non-financial resources, taking into account factors such as the nature and complexity of the

[141] 17 CFR 240.15Fh–3(h)(2)(iii)(I).

[142] *See* SIFMA 5/3/2021 Letter at 20–21 and Appendix A part (d)(3).

[143] *See* Better Markets Letter at 2.

[144] *See* SIFMA 5/3/2021 Letter Appendix A part (b)(1).

[145] *See* SIFMA 5/3/2021 Letter Appendix A part (b)(1).

[146] *See* SIFMA 5/3/2021 Letter Appendix A part (b)(1) n.2.

[147] *See* SIFMA 5/3/2021 Letter Appendix A part (b)(1).

[148] The FCA also recommended that the Commission delete from the Order the requirement for a Covered Entity to be subject to and comply with provisions of FCA SYSC 19D and PRA Remuneration Rule 6.2 (along with corollary provisions of FCA SYSC 19A applicable to IFPRU firms) as a condition to substituted compliance for internal risk management requirements. *See* FCA Comments (stating that ''these provisions appear in excess of what is strictly required for substituted compliance with the US provision'').

Covered Entity's regulated activities, the nature and scale of the business, and the risks to the continuity of the Covered Entity's services. To have appropriate non-financial resources, the Covered Entity in particular must have resources to identify, monitor, measure, and take action to remove or reduce risks to the accuracy of the Covered Entity's valuation of its assets and liabilities, be managed to a reasonable standard of effectiveness and have non-financial resources sufficient to enable it to comply with applicable requirements of the PRA. PRA Fundamental Rules 3 through 6 similarly require the Covered Entity to act in a prudent manner, maintain adequate financial resources at all times, have effective risk strategies and risk management systems and organize and control its affairs responsibly and effectively.

- UK CRR article 286 requires a Covered Entity to establish and maintain a counterparty credit risk management framework, including policies, processes, and systems to ensure the identification, measurement, approval, and internal reporting of counterparty credit risk and procedures for ensuring that those policies, processes, and systems are complied with. UK CRR article 287 addresses the internal governance of risk control and collateral management functions for Covered Entities that use internal models to calculate capital requirements. UK CRR article 288 requires the Covered Entity to conduct regular, independent reviews of its counterparty credit risk management systems and any risk control and collateral management functions required by UK CRR article 287. UK CRR article 293 addresses internal governance of the Covered Entity's internal risk management systems and validation of risk models that the Covered Entity uses.
- UK EMIR Margin RTS article 2 requires counterparties to non-centrally cleared OTC derivative contracts to establish, apply, and document risk management procedures for the exchange of collateral.
- UK MiFID Org Reg article 21 [149] addresses a Covered Entity's systems, internal controls, and arrangements for management of a variety of risk areas, including internal decision-making, allocation, proper discharge of responsibilities, compliance with decisions and internal procedures, employment of personnel able to discharge their responsibilities, internal reporting and communication of information, adequate and orderly recordkeeping, safeguarding information, business continuity, and accounting policies and procedures, as well as regular evaluation of the adequacy and effectiveness of those systems, internal controls, and arrangements. UK MiFID Org Reg article 22 addresses a Covered Entity's policies and procedures for detecting and minimizing risk of failure to comply with its obligations under UK provisions that implement MiFID, as well as the Covered Entity's independent compliance function that monitors and assesses the adequacy and effectiveness of those policies and procedures. UK MiFID Org Reg article 24 addresses a Covered Entity's internal audit function that evaluates the adequacy and effectiveness of the Covered Entity's systems, internal controls, and arrangements.

Taken as a whole, these UK requirements help to produce regulatory outcomes comparable to Exchange Act requirements to establish robust and professional internal risk management systems adequate for managing the Covered Entity's day-to-day business. The comparability analysis requires consideration of Exchange Act requirements as a whole against analogous UK requirements as a whole, recognizing that U.S. and non-U.S. regimes may follow materially different approaches in terms of specificity and technical content. This ''as a whole'' approach—which the Commission is following in lieu of requiring requirement-by-requirement similarity—further means that the conditions to substituted compliance should encompass all UK requirements that establish comparability with the applicable regulatory outcome, and helps to avoid ambiguity in the application of substituted compliance. It would be inconsistent with the holistic approach to excise relevant requirements and leave only the residual UK provisions that most closely resemble the analogous Exchange Act requirements.[150] Moreover, because Exchange Act internal risk management requirements serve the purpose of establishing internal systems to manage the Covered Entity's risks, including risks of non-compliance with applicable laws, it would be paradoxical to conclude that an SBS Entity that fails to implement requisite internal supervision practices nonetheless may be considered to be following internal risk management standards that are sufficient to meet the regulatory outcomes required under the Exchange Act; an internal supervision-related failure necessarily also constitutes a risk management failure. For these reasons, the Commission concludes that these UK provisions appropriately constitute part of the substituted compliance conditions for internal risk management requirements and is retaining the references to these provisions. In reaching this conclusion, the Commission emphasizes the importance of ensuring that substituted compliance is grounded on the comparability of regulatory outcomes. Retaining the conditions of the Order related to these UK provisions also should address another commenter's concern that any substituted compliance determination not weaken the internal risk management conditions in the proposed Order.[151]

In addition, the Commission is adding a requirement for a Covered Entity using substituted compliance for internal risk management requirements to be subject to and comply with provisions that implement MiFID articles 16 and 23, provisions of UK MiFID Org Reg related to MiFID articles 16 and 23, and provisions that implement CRD articles 88(1), 91(1), (2), and (7) through (9), 92, 94, and 95.[152] These provisions address additional aspects of a Covered Entity's management of the risks posed by internal governance and organization, business operations, conflicts of interest with and between clients, and senior staff remuneration policies. In deciding to make a positive substituted compliance determination for UK internal risk management requirements, the Commission considers that the Order's condition requiring a Covered Entity to be subject to and comply with all of the UK internal risk management requirements listed in paragraph (b)(1) of the Order help to produce regulatory outcomes comparable to Exchange Act internal risk management requirements. In deciding to make a positive substituted compliance determination for UK internal risk management requirements, the Commission considers that the Order's condition requiring a Covered Entity to be subject to and comply with all of the UK requirements listed in paragraph (b)(1)

[149] The commenter stated that these requirements are more appropriately addressed in connection with substituted compliance for internal supervision and chief compliance officer requirements. As discussed below, the Commission believes that these UK requirements are relevant to substituted compliance for Exchange Act internal risk management requirements.

[150] The Commission further believes that those conditions to substituted compliance do not expand the scope of Exchange Act requirements because substituted compliance is an option available to non-U.S. person SBS Entities—not a mandate.

[151] *See* Better Markets Letter at 2.

[152] *See* para. (b)(1) of the Order.

of the Order help to produce regulatory outcomes comparable to Exchange Act internal risk management requirements. The Commission recognizes that some of the UK requirements related to internal risk management follow a more granular approach than the high-level approach of Exchange Act internal risk management requirements, but these UK requirements, taken as a whole, are crafted to promote a Covered Entity's risk management. Within the requisite outcomes-oriented approach for analyzing comparability, the Commission concludes that a Covered Entity's failure to comply with any of those UK internal risk management requirements would be inconsistent with a Covered Entity's obligations under Exchange Act internal risk management requirements and that compliance with the full set of UK internal risk management requirements listed in paragraph (b)(1) of the Order would promote comparable regulatory outcomes.

2. Trade Acknowledgement and Verification

The Commission continues to believe that UK trade acknowledgment and verification requirements promote regulatory outcomes comparable to Exchange Act requirements, and is making a positive substituted compliance determination for trade acknowledgment and verification requirements consistent with the proposed Order. The Commission details below its consideration of comments received.

One commenter stated that the Commission inappropriately attempted to compensate for inadequate UK trade acknowledgment and verification requirements by relying on guidance.[153] The same commenter stated that, if the Commission nevertheless makes a positive substituted compliance determination, it must at a minimum ensure that the conditions in the proposed Order ''are applied with full force and without exceptions or dilution.'' [154] The commenter misinterpreted the role of guidance in the Commission's comparability analysis.

UK EMIR article 11 requires ''financial counterparties'' and ''non-financial counterparties'' to ensure appropriate procedures and arrangements are in place to achieve timely confirmation of the terms of an OTC derivative contract.[155] Similarly, UK EMIR RTS article 12 requires non-centrally cleared OTC derivative contracts between ''financial counterparties'' and ''non-financial counterparties'' to be confirmed.[156] These counterparty categories do not include entities organized outside the UK, such as U.S. persons.[157] Confirmation means the documentation of the agreement of the counterparties to all the terms of the OTC derivative contract.[158] The UK requirements as a whole thus require a Covered Entity [159] to provide a confirmation that serves as a trade acknowledgment, without regard to where its counterparty is organized, and also require the Covered Entity's counterparty, when it is a financial counterparty or non-financial counterparty, to provide a confirmation that serves as the trade verification, and the Commission considers these requirements to promote regulatory outcomes comparable to Exchange Act trade acknowledgment and verification requirements for those counterparties. The UK requirements in most instances do not require a Covered Entity's counterparty that is organized outside the UK to provide a confirmation that serves as the Exchange Act trade verification,[160] though they do require the Covered Entity to confirm the transaction.[161] Confirmation is defined as documenting the agreement of the Covered Entity and its counterparty to all the terms of the OTC derivative contract.[162]

To confirm that the Commission's analysis of the UK requirements for OTC derivatives contracts with non-UK-organized counterparties is consistent with the FCA's view of these requirements, the Commission considered the requirements together with guidance on this exact point from the FCA and ESMA.[163] In interpreting EU confirmation requirements that are identical to the relevant UK requirements, ESMA's guidance provides that ''when an EU counterparty is transacting with a third country entity, the EU counterparty would be required to ensure that the requirements for . . . timely confirmation . . . are met for the relevant . . . transactions even though the third country entity would not itself be subject to EMIR.'' [164] That guidance also provides that compliance with the EMIR confirmation requirements means ''reach[ing] a legally binding agreement to all the terms of an OTC derivative contract.'' [165] The FCA has published guidance indicating that ESMA's guidance ''will remain relevant [after the UK's exit from the EU] to the FCA and market participants in their compliance with regulatory requirements.'' [166] This

[153] *See* Better Markets Letter at 5–6 (arguing that the Commission's reliance ''on multiple layers of non-binding guidance, one of which is issued by a jurisdiction the UK does not belong to, one of which is so vague as to border on useless, would be an abdication of the SEC's responsibility to protect the U.S. financial system'').

[154] *See* Better Markets Letter at 2.

[155] *See* UK EMIR article 11(1)(a).

[156] *See* UK EMIR RTS articles 12(1) and (2).

[157] *See* UK EMIR article 2(8) (definition of ''financial counterparty''); UK EMIR article 2(9) (definition of ''non-financial counterparty'').

[158] *See* UK EMIR RTS article 1(c).

[159] The Order defines a Covered Entity to include a MiFID investment or a third country investment firm. A MiFID investment firm is included in the definition of ''financial counterparty,'' so a Covered Entity that is a MiFID investment firm is also a financial counterparty and thus is ''subject to'' UK EMIR article 11 and related provisions of UK EMIR RTS and UK EMIR Margin RTS for purposes of the Order. A third country investment firm is not included in the definitions of ''financial counterparty'' or ''non-financial counterparty,'' but may nevertheless be ''subject to'' UK EMIR article 11 and related provisions of UK EMIR RTS and UK EMIR Margin RTS for purposes of the Order if its OTC derivative contract would be subject to those obligations if it were established in the UK and either the contract has a direct, substantial, and foreseeable effect within the UK or applying UK EMIR article 11 is necessary or appropriate to prevent evasion of UK EMIR. *See* UK EMIR article 11(12).

[160] *See* UK EMIR article 2(8) (definition of ''financial counterparty'' limited to entities defined or authorized in a manner that in most instances is reserved for UK-established entities); UK EMIR article 2(9) (definition of ''non-financial counterparty'' limited to UK-established entities); UK EMIR article 11(1)(a), 11(12) (confirmation requirement applies to financial counterparties, non-financial counterparties, and third-country entities that would be subject to the confirmation requirement if established in the UK and either the relevant contract has a direct, substantial, and foreseeable effect in the UK or the obligation is necessary or appropriate to prevent the evasion of any provision of UK EMIR).

[161] Paragraph (b)(2) of the Order requires the Covered Entity to be subject to and comply with UK EMIR-based trade acknowledgment and verification requirements. A Covered Entity will be subject to those requirements only if it is a financial counterparty, non-financial counterparty, or third-country entity that would be subject to the confirmation requirement if established in the UK and either the relevant contract has a direct, substantial, and foreseeable effect in the UK or the obligation is necessary or appropriate to prevent the evasion of any provision of UK EMIR. *See* UK EMIR article 11(1)(a), 11(12).

[162] *See* UK EMIR RTS article 1(c).

[163] *See* European Securities and Markets Authority, Questions and Answers: Implementation of the Regulation (EU) No 648/2012 on OTC Derivatives, Central Counterparties and Trade Repositories (EMIR), available at: *https://www.esma.europa.eu/sites/default/files/library/esma70-1861941480-52_qa_on_emir_implementation.pdf* (''ESMA EMIR Q&A'').

[164] *See* ESMA EMIR Q&A, OTC Answer 12(b).

[165] *See* ESMA EMIR Q&A, OTC Answer 5(a).

[166] *See* Financial Conduct Authority, ''Brexit: our approach to EU non-legislative materials,'' para. 9, available at: *https://www.fca.org.uk/publication/corporate/brexit-our-approach-to-eu-non-legislative-materials.pdf* (''FCA Brexit Guidance''); *see also* FCA Brexit Guidance at para. 12 (''We will continue to have regard to other EU non-legislative material where and if they are relevant, taking account of Brexit and ongoing domestic legislation. Firms, market participants and stakeholders should also continue to do so.'').

guidance thus is consistent with the Commission's analysis of the legally binding UK requirements discussed above, and provides the Commission additional comfort that its analysis of complex UK requirements is consistent with the FCA's view of those requirements. For these reasons, the Commission disagrees with the commenter and believes that the UK trade acknowledgment and verification requirements promote regulatory outcomes comparable to Exchange Act requirements.

The Commission agrees with the comments in the Better Markets Letter that the proposed conditions to substituted compliance for trade acknowledgment and verification requirements should be retained. To further ensure that a Covered Entity using substituted compliance for trade acknowledgment and verification requirements will be required to document the agreement of the counterparties to all the terms of the relevant transaction, the Commission is issuing the Order as proposed with general conditions that will require the Covered Entity to treat its counterparty as a counterparty with whom UK trade acknowledgment and verification requirements require the Covered Entity to reach an agreement to all the terms of the OTC derivative contract and to ensure that the relevant security-based swap is either non-centrally cleared and subject to UK EMIR or centrally cleared by a UK central counterparty.[167]

Another commenter expressed general support for the proposed approach toward substituted compliance for the risk control provisions, but requested that the Commission not require a Covered Entity to be subject to and comply with UK EMIR RTS article 12(4) because it does not relate to and goes beyond Exchange Act trade acknowledgment and verification requirements.[168] As part of the UK's framework for trade acknowledgment and verification, UK EMIR RTS article 12(4) requires a Covered Entity to have the necessary procedure to report on a monthly basis to the FCA the number of unconfirmed, non-centrally cleared OTC derivative transactions that have been outstanding for more than five business days. Though Exchange Act rule 15Fi–2 does not have a similar requirement to report unconfirmed trades, the Commission considers that UK EMIR RTS article 12(4)'s requirement to report unconfirmed trades to the FCA is an inseparable part of the UK's framework for trade acknowledgment and verification, as those reports support the UK framework's mandate to confirm transactions. Requiring a Covered Entity to be subject to and comply with UK EMIR RTS article 12(4) thus is consistent with a holistic approach for comparing regulatory outcomes that reflects the whole of a jurisdiction's relevant requirements. Accordingly, the Order retains as a condition to substituted compliance for trade acknowledgment and verification requirements the requirement that the Covered Entity be subject to and comply with the entirety of UK EMIR RTS article 12.

In summary, the Commission continues to believe that UK requirements promote the goal of avoiding legal and operational risks through requirements for written records of transactions and procedures to avoid disagreements regarding the meaning of transaction terms, in a manner that is comparable to the purpose of Exchange Act rule 15Fi–2. The Commission is retaining the proposed conditions to substituted compliance for trade acknowledgment and verification, consistent with the approach advocated by a commenter.[169] While the Commission recognizes the differences between UK requirements and Exchange Act trade acknowledgment and verification requirements, in the Commission's view those differences on balance would not preclude substituted compliance, particularly as requirement-by-requirement similarity is not needed for substituted compliance. The commenter's request for a ''well-supported, evidence-based determination'' has been met here in the context of the requisite holistic analysis,[170] and the commenter's suggestion that there is a need for analysis regarding protection of the American financial system has been addressed above.[171]

3. Portfolio Reconciliation and Dispute Reporting

One commenter expressed general support for the proposed approach toward substituted compliance for the risk control provisions.[172] Another commenter stated that, if the Commission makes a positive substituted compliance determination, it must at a minimum ensure that the conditions in the proposed Order ''are applied with full force and without exceptions or dilution.'' [173] The Commission continues to believes that UK portfolio reconciliation and dispute reporting requirements promote regulatory outcomes comparable to Exchange Act requirements, by subjecting Covered Entities to risk mitigation practices that are appropriate to the risks associated with their security-based swap businesses, and is making a positive substituted compliance determination for portfolio reconciliation and dispute reporting requirements consistent with the proposed Order.[174] Substituted compliance in connection with the dispute reporting requirements is conditioned in part on the Covered Entities providing the Commission with reports regarding disputes between counterparties on the same basis as the entities provide those reports to competent authorities pursuant to UK law, to allow the Commission to obtain notice regarding key information in a manner that makes use of existing obligations under UK law.[175]

4. Portfolio Compression

One commenter expressed general support for the proposed approach toward substituted compliance for the risk control provisions.[176] Another commenter stated that, if the Commission makes a positive substituted compliance determination, it must at a minimum ensure that the conditions in the proposed Order ''are applied with full force and without exceptions or dilution.'' [177] The

[167] *See* paras. (a)(13) and (a)(14) of the Order.

[168] *See* SIFMA 5/3/2021 Letter at 9 and Appendix A part (b)(2).

[169] *See* Better Markets Letter at 2.

[170] *See* Better Markets Letter at 4 (requesting the Commission make a ''well-supported, evidence-based determination''). As discussed in part II.C.1 above, the Commission believes that the present approach toward comparability analyses—which are based on a close reading of relevant foreign requirements and careful consideration of regulatory outcomes—appropriately reflects the holistic comparability approach and the rejection of requirement-by-requirement similarity.

[171] *See* Better Markets Letter at 3–4 (stating that the Commission must provide analysis that the substituted compliance determination would protect the American financial system). As discussed in part II.C.1 above, the Commission believes that additional conditions related to protection of the American financial system would not be useful.

[172] *See* SIFMA 5/3/2021 Letter at 9.

[173] *See* Better Markets Letter at 2.

[174] *See* para. (b)(3) of the Order.

[175] *See* para. (b)(3)(ii) of the Order. The Commission recognizes the differences between the two sets of requirements—under which Exchange Act rule 15Fi–3 requires SBS Entities to report valuation disputes in excess of $20 million that have been outstanding for three or five business days (depending on counterparty types), while UK EMIR RTS article 15(2) requires firms to report disputes between counterparties in excess of €15 million and outstanding for at least 15 business days. In the Commission's view, the two requirements produce comparable regulatory outcomes notwithstanding those differences.

[176] *See* SIFMA 5/3/2021 Letter at 9.

[177] *See* Better Markets Letter at 2.

Commission continues to believe that UK portfolio compression requirements promote regulatory outcomes comparable to Exchange Act requirements, by subjecting Covered Entities to risk mitigation practices that are appropriate to the risks associated with their security-based swap businesses, and is making a positive substituted compliance determination for portfolio compression requirements consistent with the proposed Order.[178]

5. Trading Relationship Documentation

The Commission continues to believe that UK trading relationship documentation requirements promote regulatory outcomes comparable to Exchange Act requirements, and is making a positive substituted compliance determination for trading relationship documentation requirements consistent with the proposed Order. The Commission details below its consideration of comments received.

One commenter stated that the Commission inappropriately attempted to compensate for inadequate UK trading relationship documentation requirements by relying on guidance.[179] The same commenter stated that, if the Commission nevertheless makes a positive substituted compliance determination, it must at a minimum ensure that the conditions in the proposed Order ''are applied with full force and without exceptions or dilution.'' [180] The commenter misinterpreted the role of guidance in the Commission's comparability analysis. The proposed Order would require a Covered Entity to be subject to and comply with UK EMIR article 11(1)(a), UK EMIR RTS article 12, and UK EMIR Margin RTS article 2. The Commission highlights the special importance of UK EMIR Margin RTS article 2, which addresses risk management procedures related to the exchange of collateral, including procedures related to the terms of all necessary agreements to be entered into by counterparties (*e.g.,* payment obligations, netting conditions, events of default, calculation methods, transfers of rights and obligations upon termination, and governing law). Those obligations are denoted as being connected to collateral exchange obligations, and the Commission believes that they are necessary to help produce a regulatory outcome that mitigates risk in a manner that is comparable to the outcome associated with the Exchange Act trading relationship documentation requirements. To bridge any gap left by UK EMIR Margin RTS article 2, the Commission is also requiring compliance with UK EMIR article 11(1)(a) and UK EMIR RTS article 12, which, as discussed in part IV.B.2 above, require the Covered Entity to confirm the transaction, with confirmation defined as documentation of the agreement of the counterparties to all the terms of the OTC derivative contract. Also as discussed in part IV.B.2 above, the Commission consulted guidance from the FCA and ESMA to confirm that the Commission's analysis of those complex UK requirements was consistent with the FCA's view of those requirements.[181] The Commission thus agrees with the commenter that the proposed conditions to substituted compliance for trading relationship documentation requirements should be retained. To further ensure that a Covered Entity using substituted compliance for trading relationship documentation requirements will be required to document the agreement of the counterparties to all the terms of the relevant transaction, the Commission is issuing the Order as proposed with two general conditions that will require the Covered Entity to treat its counterparty as a financial counterparty or non-financial counterparty when complying UK trade acknowledgment and verification requirements.[182]

Another commenter expressed general support for the proposed approach toward substituted compliance for the risk control provisions, but requested that the Commission not require a Covered Entity to be subject to and comply with UK EMIR RTS article 12(4) because it does not relate to and goes beyond Exchange Act trading relationship documentation requirements.[183] For the reasons described in part IV.B.2 above, the Commission is retaining the reference to this provision.

Accordingly, the Commission continues to believe that UK requirements promote regulatory outcomes comparable to Exchange Act trading relationship documentation requirements. While the Commission recognizes that these and certain other differences between UK requirements and Exchange Act trading relationship documentation requirements, in the Commission's view those differences on balance would not preclude substituted compliance, particularly as requirement-by-requirement similarity is not needed for substituted compliance.

V. Substituted Compliance for Capital and Margin Requirements

A. Proposed Approach

The FCA Application in part requested substituted compliance in connection with capital and margin requirements relating to:

- *Capital*—Capital requirements pursuant to Exchange Act section 15F(e) and Exchange Act rule 18a–1 and its appendices (collectively ''Exchange Act rule 18a–1'') applicable to certain SBS Entities.[184] Exchange Act rule 18a–1 helps to ensure the SBS Entity maintains at all times sufficient liquid assets to promptly satisfy its liabilities, and to provide a cushion of liquid assets in excess of liabilities to cover potential market, credit, and other risks. The rule's net liquid assets test standard protects customers and counterparties and mitigates the consequences of an SBS Entity's failure by promoting the ability of the firm to absorb financial shocks and, if necessary, to self-liquidate in an orderly manner.[185] As part of the capital requirements, security-based swap dealers without a prudential regulator also must comply with the internal risk management control requirements of Exchange Act

[178] *See* para. (b)(4) of the Order.

[179] *See* Better Markets Letter at 5–6.

[180] *See* Better Markets Letter at 2.

[181] *See* ESMA EMIR Q&A, OTC Answers 5(a), 12(b); FCA Brexit Guidance at paras. 9, 12.

[182] *See* para. (a)(13) of the Order.

[183] *See* SIFMA 5/3/2021 Letter at 9 and Appendix A part (b)(5).

[184] 17 CFR 240.18a–1 through 18a–1d. Exchange Act rule 18a–1 applies to security-based swap dealers that: (1) Do not have a prudential regulator and (2) are either: (a) Not dually registered with the Commission as a broker-dealer; or (b) are dually registered with the Commission as a special purpose broker-dealer known as an OTC derivatives dealer. Security-based swap dealers that are dually registered with the Commission as a full-service broker-dealer are subject to the capital requirements of Exchange Act rule 15c3–1 (17 CFR 240.15c3–1) for which substituted compliance is not available. *See* 17 CFR 240.3a71–6(d)(4)(i) (making substituted compliance available only with respect to the capital requirements of Exchange Act section 15F(e) and Exchange Act rule 18a–1).

[185] *See* Exchange Act Release No. 86175 (June 21, 2019), 84 FR 43872, 43879–83 (Aug. 22, 2019) (''Capital and Margin Adopting Release''). The capital standard of Exchange Act rule 18a–1 is based on the net liquid assets test of Exchange Act rule 15c3–1 applicable to broker-dealers. *See* Capital and Margin Adopting Release, 84 FR 43872, 43879–83. The net liquid assets test seeks to promote liquidity by requiring that a firm maintain sufficient liquid assets to meet all liabilities, including obligations to customers, counterparties, and other creditors, and, in the event a firm fails financially, to have adequate additional resources to wind-down its business in an orderly manner without the need for a formal proceeding. *See* Capital and Margin Adopting Release, 84 FR at 43879. *See* FCA Application Appendix B, Annex V (Side Letter Addressing Capital Requirements).

rule 15c3–4 with respect to certain activities.[186]

• *Margin*—Margin requirements pursuant to Exchange Act section 15F(e) and Exchange Act rule 18a–3 for non-prudentially regulated SBS Entities.[187] The margin requirements are designed to protect SBS Entities from the consequences of a counterparty's default.[188]

Taken as a whole, these capital and margin requirements help to promote market stability by mandating that SBS Entities follow practices to manage the market, credit, liquidity, solvency, counterparty, and operational risks associated with their security-based swap businesses.

In proposing to provide conditional substituted compliance in connection with this part of the FCA Application, the Commission preliminarily concluded that substituted compliance with respect to the Exchange Act capital requirements would be subject to certain additional conditions.[189] The conditions were designed to help ensure the comparability of regulatory outcomes between Exchange Act rule 18a–1 (which imposes a net liquid assets test) and the capital requirements applicable to nonbank security-based swap dealers in the UK that are expected to register with the Commission. Those capital requirements are based on the international capital standard for banks (''Basel capital standard'').[190]

In proposing to provide conditional substituted compliance in connection with this part of the FCA Application, the Commission preliminarily concluded that relevant UK margin requirements would produce regulatory outcomes that are comparable to those associated with the Exchange Act margin requirements.[191]

Finally, the proposed Order would permit a Covered Entity to apply substituted compliance for the capital *and/or* margin requirements.[192] Thus, a Covered Entity could apply substituted compliance for Exchange Act margin requirements by complying with UK margin requirements but comply with Exchange Act capital requirements (rather than applying substituted compliance to those requirements) and vice versa. However, as to the various requirements within the capital and margin rules, the Commission found the rules to be entity-level when adopting amendments to Exchange Act rule 3a71–6 to make substituted compliance available with respect to them. Consequently, under the proposed Order, a Covered Entity must apply substituted compliance with respect to capital and margin requirements at an entity level.

B. Commenter Views and Final Provisions

1. Capital

Consistent with the proposed Order, the first capital condition requires the covered entity to be subject to and comply with certain identified UK capital requirements.[193] As discussed at the end of this section, the Commission made some modifications to the UK laws and regulations cited in this condition.[194] For the reasons discussed below, there are two additional conditions to applying substituted compliance with respect to Exchange Act rule 18a–1.

For the reasons discussed above in part III.B.2.k of this release, the first additional capital condition is that the Covered Entity applies substituted compliance with respect to Exchange Act rules 18a–5(a)(9) (a record making requirement), 18a–6(b)(1)(x) (a record preservation requirement), and 18a–8(a)(1)(i), (a)(1)(ii), (b)(1), (b)(2), and (b)(4) (notification requirements).[195] These recordkeeping and notification requirements are directly linked to the capital requirements of Exchange Act rule 18a–1. The proposed Order conditioned substituted compliance with respect to these recordkeeping and notification requirements on the Covered Entity applying substituted compliance with respect to Exchange Act rule 18a–1.[196] This additional capital condition is designed to provide clarity as to the Covered Entity's obligations under these recordkeeping and notification requirements when applying substituted compliance with respect to Exchange Act rule 18a–1 pursuant this Order.

The second additional capital condition builds on and modifies the proposed capital condition that was designed to address potential different regulatory outcomes between Exchange Act rule 18a–1and the UK capital requirements. In particular, the Commission proposed a four pronged condition with respect to applying substituted compliance to the capital requirements of Exchange Act rule 18a–1.[197] The first prong would require a Covered Entity to maintain an amount of assets that are allowable under Exchange Act rule 18a–1, after applying applicable haircuts under the Basel capital standard, that equals or exceeds the Covered Entity's current liabilities coming due in the next 365 days.[198] The second prong was linked to the first prong as it would require that a Covered Entity make a quarterly record listing: (1) The assets maintained pursuant to the first prong, their value, and the amount of their applicable haircuts; and (2) the aggregate amount of the liabilities coming due in the next 365 days. The third prong would require the Covered Entity to maintain at least $100 million of equity capital composed of highly liquid assets as defined in the Basel capital standard. The fourth prong would require the Covered Entity to include its most recently filed statement of financial condition whether audited or unaudited with its initial notice to the Commission of its intent to rely on substituted compliance.

One commenter recommended that the Commission consider denying substituted compliance for capital requirements on the basis that the UK's capital requirements do not produce comparable regulatory outcomes.[199] This commenter stated that ''granting substituted compliance with multiple conditions intended to mimic the Commission's capital requirements would seem to undermine the entire point of substituted compliance in the first place; namely, protecting the stability of the U.S. financial system by allowing substituted compliance *only*

[186] *See* 17 CFR 240.15c3–4 and 18a–1(f).

[187] 17 CFR 240.18a–3.

[188] *See* Capital and Margin Adopting Release, 84 FR at 43947, 43949 (''Obtaining collateral is one of the ways OTC derivatives dealers manage their credit risk exposure to OTC derivatives counterparties. Prior to the financial crisis, in certain circumstances, counterparties were able to enter into OTC derivatives transactions without having to deliver collateral. When ''trigger events'' occurred during the financial crisis, those counterparties faced significant liquidity strains when they were required to deliver collateral'').

[189] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18385–89, 18413.

[190] *See, e.g.,* Basel Committee on Banking Supervision (''BCBS''), The Basel Framework, available at: *https://www.bis.org/basel_framework/*.

[191] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18386, 18413.

[192] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18386–87.

[193] *See* para. (c)(1)(i) of the Order. *See also* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18386.

[194] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18386, n.81.

[195] *See* para. (c)(1)(ii) of the Order.

[196] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18395–18403, 18416–17, 19419.

[197] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18387–89 (discussing the additional conditions).

[198] As used in this part V.B.1. of the release, the term ''Covered Entity'' refers to a security-based swap dealer located in the UK that does not have a prudential regulator.

[199] *See* Better Markets Letter at 8.

when foreign regimes are comparable.'' [200]

In describing the differences in the capital frameworks between the net liquid assets test and the Basel capital standard, this commenter highlighted the treatment of initial margin posted to a counterparty.[201] Specifically, the commenter stated that in the UK initial margin posted to a counterparty counts as capital for that entity, while in the U.S. initial margin only counts as capital if the security-based swap dealer has a special loan agreement with an affiliate. The commenter stated that the U.S. requirement is intended to mitigate counterparty credit risk with respect to the return of the initial margin. The commenter argued that the result is that, not only are the UK requirements different from the Commission's in both form and substance, but the regulatory outcome is not comparable.

This commenter also stated that if a positive substituted compliance determination is made regarding capital, the Commission should not weaken the proposed additional capital condition in response to industry commenters, because these market participants are primarily concerned with reducing their own operational costs, without any regard to the systemic risk that would doing so would pose.[202] This commenter also stated that any determination to find the UK's capital requirements comparable to and as comprehensive as the Commission's capital framework without conditions at least as strong as proposed would not only contravene the Commission's own conception of substituted compliance ''but expose the U.S. financial system to very risks Dodd-Frank instructed the SEC to contain.'' [203]

Another commenter supported the proposed additional capital condition.[204] This commenter stated that the Commission should require Covered Entities to comply with the net liquid assets test under Exchange Act rule 18a–1, rather than the Basel capital standards.[205] The commenter stated that the net liquid assets test ''appropriately limits uncollateralized lending, fixed assets, and other illiquid assets such as real estate which have been proven repeatedly to be unreliable forms of capital but are currently counted'' as allowable capital under the Basel capital standard.[206] This commenter also agreed with the Commission that ''the initial margin that is posted is not available for other purposes and therefore, under the Basel standard, could swiftly result in less balance sheet liquidity than the standards under the Exchange Act's Rule 18a–1.'' [207]

A commenter supported the Commission's proposed Order to grant substituted compliance in connection with the Exchange Act capital requirements.[208] This commenter, however, opposed the proposed additional four pronged capital condition. The commenter stated that it was unnecessary, unduly rushed, and highly likely to be costly and disruptive to market participants and inconsistent with the Commission's substituted compliance framework.[209] More specifically, this commenter stated that the proposed capital condition was unnecessary because Covered Entities transact predominantly in securities and derivatives, do not extensively engage in unsecured lending or other activities more typical of banks, and are already subject to extensive liquidity requirements.[210] The commenter also expressed concern that the proposed capital condition was inconsistent with the Commission's substituted compliance framework in that it was duplicative of and would contradict the liquidity requirements established by the PRA.[211] This commenter stated that the imposition of the proposed capital condition would effectively substitute the Commission's judgment for the PRA's in terms of the best way to address liquidity risk, and may lead other regulators to refuse to extend deference to the Commission's regulatory determinations.[212]

With respect to the using the concept of ''allowable'' and ''nonallowable'' assets under Exchange Act rule 18a–1, the commenter stated that the first and second prongs of the capital condition do not define these terms and there is no analogous concept in the capital framework applicable in the UK.[213] The commenter stated this would require firms to re-categorize every asset on their balance sheets, which would not be feasible in the near term.[214] Further, this commenter asked the Commission to clarify what it means by ''haircuts'' with respect to the first and second prongs, since the Basel capital standard does not apply ''haircuts'' to assets, but instead applies a risk-weighted approach.[215]

This commenter also stated that the third prong of the proposed additional capital condition requiring ''at least $100 million of equity capital composed of 'highly liquid assets' as defined in the Basel capital standard,'' includes concepts that require clarification.[216] For example, this commenter stated that is unclear how a firm would calculate the amount of its ''equity capital'' that is ''composed of highly liquid assets,'' since ''equity'' generally refers to a firm's paid-in capital, retained earnings, and other items on the liabilities/shareholders' equity side of the balance sheet.[217] Finally, this commenter asserted that because it is approximately three months until the August 6th counting date, and firms may encounter significant operational challenges to meet the proposed or revised capital condition, the proposed condition may cause firms to exit the U.S. security-based swap market, or hope that the conditions are modified and delayed in a manner that will make it feasible to satisfy them.[218]

Overall, this commenter stated that the Commission should take a more incremental and deliberative approach to additional capital conditions, and specifically recommended that the Commission: (1) Delete the first prong of the capital condition; (2) replace the second prong with a requirement that a nonbank Covered Entity provide the same reports concerning liquidity metrics that the Covered Entity provides to the PRA; (3) modify the third prong to require a nonbank Covered Entity to maintain at least $100 million of high quality liquid assets, as defined in the Basel capital standard; and (4) issue an order on October 6, 2024, determining whether to maintain, delete, modify, or supplement the condition, based on consideration of the liquidity of nonbank Covered Entities, and after publishing a notice of any such changes

[200] Better Markets Letter at 8 (emphasis in the original).

[201] Better Markets Letter at 7.

[202] Better Markets Letter at 7–8.

[203] Better Markets Letter at 7–8.

[204] *See* Letter from Americans for Financial Reform Education Fund (May 3, 2021) (''Americans for Financial Reform Education Fund Letter'') at 1.

[205] *See* Americans for Financial Reform Education Fund Letter at 1 (''We support the Commission's proposal to require foreign security-based swap dealers and participants (''Covered Entities'') to abide by capital and initial margin requirements that reflect Exchange Act rule 18a–1 standards appropriate for broker-dealers, as opposed to Basel capital requirements for banks that permit illiquid assets to count toward capital minimums.'').

[206] *See* Americans for Financial Reform Education Fund Letter at 1.

[207] *See* Americans for Financial Reform Education Fund Letter at 2.

[208] SIFMA 5/3/2021 Letter at 10.

[209] SIFMA 5/3/2021 Letter at 10, 17.

[210] SIFMA 5/3/2021 Letter at 10–15.

[211] SIFMA 5/3/2021 Letter at 15.

[212] SIFMA 5/3/2021 Letter at 15–17.

[213] SIFMA 5/3/2021 Letter at 17.

[214] SIFMA 5/3/2021 Letter at 17.

[215] SIFMA 5/3/2021 Letter at 17–18.

[216] SIFMA 5/3/2021 Letter at 18.

[217] SIFMA 5/3/2021 Letter at 18.

[218] SIFMA 5/3/2021 Letter at 19.

for at least 90 days of public comment.[219]

The Commission agrees with the commenters who point out the differences between the capital standard of Exchange Act rule 18a–1 (*i.e.,* the net liquid assets test) and the Basel capital standard applicable to Covered Entities, and who therefore believe that—at a minimum—additional conditions are necessary to achieve comparable regulatory outcomes.[220] As the Commission explained when proposing the additional capital condition, the net liquid assets test is designed to promote liquidity.[221] In particular, Exchange Act rule 18a–1 allows an SBS Entity to engage in activities that are part of conducting a securities business (*e.g.,* taking securities into inventory) but in a manner that places the firm in the position of holding at all times more than one dollar of highly liquid assets for each dollar of unsubordinated liabilities (*e.g.,* money owed to customers, counterparties, and creditors).[222] For example, Exchange Act rule 18a–1 allows securities positions to count as allowable net capital, subject to standardized or internal model-based haircuts. The rule, however, does not permit most unsecured receivables to count as allowable net capital. This aspect of the rule limits the ability of SBS Entities to engage in activities, such as uncollateralized lending, that generate unsecured receivables. The rule also does not permit fixed assets or other illiquid assets to count as allowable net capital, which creates disincentives for SBS Entities to own real estate and other fixed assets that cannot be readily converted into cash. For these reasons, Exchange Act rule 18a–1 incentivizes SBS Entities to confine their business activities and devote capital to security-based swap activities.

The net liquid assets test is imposed through how an SBS Entity is required to compute net capital pursuant to Exchange Act rule 18a–1. The first step is to compute the SBS Entity's net worth under U.S. generally accepted accounting principles (''GAAP''). Next, the SBS Entity must make certain adjustments to its net worth to calculate net capital, such as deducting illiquid assets and taking other capital charges and adding qualifying subordinated loans.[223] The amount remaining after these deductions is defined as ''tentative net capital.'' Exchange Act rule 18a–1 prescribes a minimum tentative net capital requirement of $100 million for SBS Entities approved to use models to calculate net capital. An SBS Entity that is meeting its minimum tentative net capital requirement will be in the position where each dollar of unsubordinated liabilities is matched by more than a dollar of highly liquid assets.[224] The final step in computing net capital is to take prescribed percentage deductions (standardized haircuts) or model-based deductions from the mark-to-market value of the SBS Entity's proprietary positions (*e.g.,* securities, money market instruments, and commodities) that are included in its tentative net capital. The amount remaining is the firm's net capital, which must exceed the greater of $20 million or a ratio amount.

In comparison, Covered Entities in the UK are subject to the Basel capital standard. The Basel capital standard counts as capital assets that Exchange Act rule 18a–1 would exclude (*e.g.,* loans and most other types of uncollateralized receivables, furniture and fixtures, real estate). The Basel capital standard accommodates the business of banking: making loans (including extending unsecured credit) and taking deposits. While the Covered Entities that will apply substituted compliance with respect to Exchange Act rule 18a–1 will not be banks, the Basel capital standard allows them to count illiquid assets such as real estate and fixtures as capital. It also allows them to treat unsecured receivables related to activities beyond dealing in security-based swaps as capital notwithstanding the illiquidity of these assets.

Further, one critical example of the difference between the requirements of Exchange Act rule 18a–1 and the Basel capital standard relates to the treatment of initial margin with respect to security-based swaps and swaps. Under the UK margin requirements, Covered Entities will be required to post initial margin to counterparties unless an exception applies.[225] Under Exchange Act rule 18a–1, an SBS Entity cannot count as capital the amount of initial margin posted to a counterparty unless it enters into a special loan agreement with an affiliate.[226] The special loan agreement requires the affiliate to fund the initial margin amount and the agreement must be structured so that the affiliate—rather than the SBS Entity—bears the risk that the counterparty may default on the obligation to return the initial margin. The reason for this restrictive approach to initial margin posted away is that it ''would not be available [to the SBS Entity] for other purposes, and, therefore, the firm's liquidity would be reduced.'' [227] Under the Basel capital standard, a Covered Entity can count initial margin posted

[219] SIFMA 5/3/2021 Letter at 19–20.

[220] *See* Americans for Financial Reform Education Fund Letter at 1–2; Better Markets Letter at 7–8.

[221] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18387 (explaining the differences between Exchange Act rule 18a–1 and the Basel capital standard).

[222] *See, e.g.,* Exchange Act Release No. 8024 (Jan. 18, 1967), 32 FR 856 (Jan. 25, 1967) (''Rule 15c3–1 (17 CFR 240.15c3–1) was adopted to provide safeguards for public investors by setting standards of financial responsibility to be met by brokers and dealers. The basic concept of the rule is liquidity; its object being to require a broker-dealer to have at all times sufficient liquid assets to cover his current indebtedness.'') (footnotes omitted); Exchange Act Release No. 10209 (June 8, 1973), 38 FR 16774 (June 26, 1973) (Commission release of a letter from the Division of Market Regulation) (''The purpose of the net capital rule is to require a broker or dealer to have at all times sufficient liquid assets to cover its current indebtedness. The need for liquidity has long been recognized as vital to the public interest and for the protection of investors and is predicated on the belief that accounts are not opened and maintained with broker-dealers in anticipation of relying upon suit, judgment and execution to collect claims but rather on a reasonable demand one can liquidate his cash or securities positions.''); Exchange Act Release No. 15426 (Dec. 21, 1978), 44 FR 1754 (Jan. 8, 1979) (''The rule requires brokers or dealers to have sufficient cash or liquid assets to protect the cash or securities positions carried in their customers' accounts. The thrust of the rule is to insure that a broker or dealer has sufficient liquid assets to cover current indebtedness.''); Exchange Act Release No. 26402 (Dec. 28, 1988), 54 FR 315 (Jan. 5, 1989) (''The rule's design is that broker-dealers maintain liquid assets in sufficient amounts to enable them to satisfy promptly their liabilities. The rule accomplishes this by requiring broker-dealers to maintain liquid assets in excess of their liabilities to protect against potential market and credit risks.'') (footnote omitted).

[223] *See* 17 CFR 240.15c3–1(c)(2).

[224] The highly liquid assets under Exchange Act rule 18a–1 are otherwise known as ''allowable assets'' because they are not deducted when computing net capital. *See* Exchange Act Release No. 87005 (Sept. 19, 2019), 84 FR 68673, 68673–74, 68677–80 (Dec. 19, 2019) (''Books and Records Adopting Release'')(the sections of the amended Part II of the FOCUS Report setting forth the assets side of the balance sheet and the net capital computation). Illiquid assets otherwise known as ''non-allowable assets'' are deducted when computing net capital. *See* Books and Records Adopting Release, 84 FR at 68673–74, 68677–80. Allowable assets include cash, certain unsecured receivables from broker-dealers and clearing organizations, reverse repurchase agreements, securities borrowed, fully secured customer margin loans, and proprietary securities, commodities, and swaps positions. *See* Books and Records Adopting Release, 84 FR at 68673–74, 68677–80. The term ''high quality liquid assets'' or ''HQLA'' are defined under the Basel capital standard's liquidity coverage ratio (''LCR'') and generally consist of cash and specific classes of liquid securities. *See* BCBS, *LCR30 under the Basel capital standards,* available at: *https://www.bis.org/basel_framework/chapter/LCR/30.htm?tldate=20191231&inforce=2019121*. Generally, cash and securities that qualify as HQLA under the LCR would be allowable assets under Exchange Act rule 18a–1.

[225] Exchange Act rule 18a–3 does not require SBS Entities to post initial margin (though it does not prohibit the practice).

[226] *See* Capital and Margin Adopting Release, 84 FR at 43887–88.

[227] *See* Capital and Margin Adopting Release, 84 FR at 43887.

away as capital without the need to enter into a special loan arrangement with an affiliate. Consequently, because of the ability to include illiquid assets and margin posted away as capital, Covered Entities subject to the Basel capital standard may have less balance sheet liquidity than SBS Entities subject to Exchange Act rule 18a–1.

For these reasons, the Commission disagrees with the commenter who stated that additional capital conditions were unnecessary and inconsistent with the Commission's substituted compliance framework.[228] As discussed above, there are key differences between the net liquid assets test of Exchange Act rule 18a–1 and the Basel capital standard applicable to Covered Entities. Those differences in terms of the types of assets that count as regulatory capital and how regulatory capital is calculated lead to different regulatory outcomes.[229] In particular, the net liquid assets test produces a regulatory outcome in which the SBS Entity has more than one dollar of highly liquid assets for each dollar of unsubordinated liabilities.[230] The Basel capital standard—while having measures designed to promote liquidity—does not produce this regulatory outcome.[231] Therefore, an additional capital condition is needed to bridge the gap between these two capital standards and thereby achieve more comparable regulatory outcomes in terms of promoting liquid balance sheets for SBS Entities and Covered Entities.

However, in seeking to bridge this regulatory gap, the additional condition should take into account that Covered Entities are or will be subject to UK laws and measures designed to promote liquidity. As a commenter stated, Covered Entities are or will be subject to: (1) Requirements to hold an amount of HQLA to meet expected payment obligations under stressed conditions for thirty days (''LCR requirement''); [232] (2) requirements to hold a diversity of stable funding instruments sufficient to meet long-term obligations under both normal and stressed conditions (''NSFR requirements''); [233] (3) requirements to perform liquidity stress tests and manage liquidity risk (''internal liquidity assessment requirements''); [234] and (4) regular PRA reviews of a Covered Entity's liquidity risk management processes (''PRA liquidity review process'').[235] These UK laws and measures will require Covered Entities to hold significant levels of liquid assets. However, the laws and measures on their own, do not impose a net liquid assets test. Therefore, an additional condition is necessary to supplement these requirements.

The Commission has taken into account the UK liquidity laws and measures discussed above in making a substituted compliance determination with respect to Exchange Act rule 18a–1, and in tailoring additional capital conditions designed to achieve comparable regulatory outcomes. The LCR, NSFR, and internal liquidity assessment requirements collectively will require Covered Entities to maintain pools of unencumbered HQLA to cover potential cash outflows during a 30-day stress period, to fund long-term obligations with stable funding instruments, and to manage liquidity risk. These requirements—coupled with the PRA's supervisory reviews of the liquidity risk management practices of Covered Entities—will require Covered Entities to hold significant levels of liquid assets. These requirements and measures in combination with the other capital requirements applicable to Covered Entities provide a starting foundation for making a positive substituted compliance determination with respect to the capital requirements of Exchange Act section 15F(e) and Exchange Act rule 18a–1.[236] However, more is needed to achieve a comparable regulatory outcome to the net liquid assets test of Exchange Act rule 18a–1.

For these reasons, the Order includes an additional capital condition that will impose a simplified net liquid assets test.[237] This simplified test will require the Covered Entity to hold more than one dollar of liquid assets for each dollar of liabilities. The simplified net liquid assets test—when coupled with the PRA capital requirements,[238] LCR requirements, NSFR requirements, internal liquidity assessment requirements, and PRA liquidity review process—is designed to produce a regulatory outcome that is comparable to the net liquid assets test of Exchange Act rule 18a–1 (*i.e.,* sufficient liquidity to cover liabilities and to promote the maintenance of highly liquid balance sheets).

In response to comments, the Commission has modified the first three prongs of the additional capital condition from the proposed Order.[239] In particular, the first and third prongs are being combined into a single prong of the second additional capital condition.[240] Under this prong, the Covered Entity must maintain liquid assets (as defined in the capital condition) that have an aggregate market value that exceeds the amount of the Covered Entity's total liabilities by at least: (1) $100 million before applying a deduction (specified in the capital condition); and (2) $20 million after applying the deduction.[241] Thus, the condition increases the scope of the liquid assets requirement so that it must

[228] SIFMA 5/3/2021 Letter at 10.

[229] *See* Better Markets Letter at 6–7 (comparing the differences between Exchange Act rule 18a–1 and the Basel capital standard and stating that ''not only are the UK's capital requirements different from the SEC's in both form and substance, but the regulatory outcome is not comparable'').

[230] As discussed above, highly liquid assets under Exchange Act rule 18a–1 are also known as ''allowable assets'' and generally are consistent the LCR's HQLA.

[231] The Basel capital standard does not preclude a firm from having more than a dollar of highly liquid assets for each dollar of unsubordinated liabilities. Thus, a firm operating pursuant to the standard may structure its assets and liabilities in a manner that achieves this result. However, the standard does not mandate this result. Rather, it will accommodate a firm that seeks to maintain this level of liquidity on its own accord.

[232] *See* Liquidity Coverage Requirement—UK Designated Investment Firms part of PRA Rulebook.

[233] *See* UK CRR, Article 413; *see also* PRA, Consultation Paper CP5/21, Implementation of Basel

Standards (February 2021) (proposed to take effect on January 1, 2022).

[234] *See* Internal Liquidity Adequacy Assessment part of the PRA Rulebook.

[235] *See* SIFMA 5/3/2021 Letter at 12–15.

[236] *See* Better Markets Letter at 8 (recommending that the Commission consider denying substituted compliance with respect to these Exchange Act capital requirements).

[237] *See* Americans for Financial Reform Education Fund Letter at 1 (''The Commission should require that SBS entities who want to operate in the U.S. comply with the Net Liquid Assets test under the Exchange Act rule 18a–1 rather than the Basel capital standards applicable under UK and EU regulations.'').

[238] *See, e.g.,* CRR, Part 1 (Own Funds, including Tier 1 capital) and Part 2 (Capital Requirements).

[239] *See* Americans for Financial Reform Education Fund Letter at 1 (''The Commission should require that SBS entities who want to operate in the U.S. comply with the Net Liquid Assets test under the Exchange Act rule 18a–1 rather than the Basel capital standards''); SIFMA 5/3/2021 Letter at 17 (raising concerns that the use of the concept of ''allowable'' assets under Exchange Act rule 18a–1 in the first condition would require Covered Entities to re-categorize every asset on their balance sheets, which also pertains to the second condition, and seeking clarification on to how to calculate ''equity capital'' and allocate it to highly liquid assets equal to or greater than $100 million).

[240] The first prong of the proposed capital condition would have required a Covered Entity to maintain an amount of assets that are allowable under Exchange Act rule 18a–1, after applying applicable haircuts under the Basel capital standard, that equals or exceeds the Covered Entity's current liabilities coming due in the next 365 days. The second prong would have required the Covered Entity to make a quarterly record related to the first prong. The third prong would have required the Covered Entity to maintain at least $100 million of equity capital composed of highly liquid assets as defined in the Basel capital standard. *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18387–88.

[241] *See* para. (c)(1)(iii)(A)(*1*) of the Order. The definition of ''liquid assets'' and the method of calculating the deductions are discussed below.

cover all liabilities (rather than those maturing in 365 days as was proposed).

These modifications align the first prong more closely to the $100 million tentative net capital requirement of Exchange Act rule 18a–1 applicable to SBS Entities approved to use models. As discussed above, Exchange Act rule 18a–1 requires SBS Entities that have been approved to use models to maintain at least *$100 million* in tentative net capital. And, tentative net capital is the amount that an SBS Entity's liquid assets exceed its total unsubordinated liabilities *before applying haircuts.* The first prong will require the Covered Entity to subtract total liabilities from total liquid assets. The amount remaining will need to equal or exceed $100 million. The modifications also align the condition more closely to the $20 million fixed-dollar minimum net capital requirement of Exchange Act rule 18a–1. As discussed above, net capital is calculated by *applying haircuts* (deductions) to tentative net capital and the fixed-dollar minimum requires that net capital must equal or exceed *$20 million.* The first prong will require the Covered Entity to subtract total liabilities from total liquid assets and then apply the deduction to the difference. The amount remaining after the deduction will need to equal or exceed $20 million.

For the purposes of the first prong of the second additional capital condition, ''liquid assets'' are defined as: (1) Cash and cash equivalents; (2) collateralized agreements; (3) customer and other trading related receivables; (4) trading and financial assets; and (5) initial margin posted by the Covered Entity to a counterparty or third-party (subject to certain conditions discussed below).[242] These categories of liquid assets are designed to align with assets that are considered allowable assets for purposes of calculating net capital under Exchange Act rule 18a–1.[243] Further, the first four categories of liquid assets also are designed to align with how Covered Entities categorize liquid assets on their financial statements.[244] In addition, a commenter submitted a table summarizing categories of liquid assets on the balance sheets of six UK dealers (''Balance Sheet Table'') that the commenter expects will register with the Commission as security-based swap dealers, and that do not have a prudential regulator and therefore would be subject to Exchange Act rule 18a–1.[245]

The first category of liquid assets is cash and cash equivalents.[246] These assets consist of cash and demand deposits at banks (net of overdrafts) and highly liquid investments with original maturities of three months or less that are readily convertible into known amounts of cash and subject to insignificant risk of change in value.[247] The second category of liquid assets is collateralized agreements.[248] These assets consist of secured financings where securities serve as collateral such as repurchase agreements and securities loaned transactions.[249] The third category of liquid assets is customer and other trading related receivables.[250] These assets consist of customer margin loans, receivables from broker-dealers, receivables related to fails to deliver, and receivables from clearing organizations.[251] The fourth category of liquid assets is trading and financial assets.[252] These assets consist of cash market securities positions and listed and over-the-counter derivatives positions.[253]

As discussed above, initial margin posted to a counterparty is treated differently under Exchange Act rule 18a–1 and the Basel capital standard, and commenters highlighted this difference.[254] The fifth category of liquid assets is initial margin posted by the Covered Entity to a counterparty or a third-party custodian, provided: (1) The initial margin requirement is funded by a fully executed written loan agreement with an affiliate of the Covered Entity; (2) the loan agreement provides that the lender waives repayment of the loan until the initial margin is returned to the Covered Entity; and (3) the liability of the Covered Entity to the lender can be fully satisfied by delivering the collateral serving as initial margin to the

[242] *See* para. (c)(1)(iii)(B) of the Order.

[243] *See supra* notes 224 and 230 (describing allowable assets under Exchange Act rule 18a–1).

[244] The Bank of England publishes a list of the investment firms that have been designated to the PRA (''PRA-designated investment firms''). This list is available at: *https://www.bankofengland.co.uk/prudential-regulation/authorisations/which-firms-does-the-pra-regulate.* As part of the application process, the FCA has stated that the only nonbank (*i.e.,* non-prudentially regulated) UK dealers that will register with the Commission as security-based swap dealers are PRA-designated investment firms. The commenter that provided the table showing the balance sheets of six UK investment firms makes the same statement. *See* SIFMA 5/3/2021 Letter Appendix A (''We expect all covered entities to be banks or PRA-designated investment firms''). According to the Bank of England, the following dealers are PRA-designated investment firms (as of January 4, 2021): Barclays Capital Securities Limited, Citigroup Global Markets Limited, Credit Suisse Securities (Europe) Ltd, Goldman Sachs International, Merrill Lynch International, MUFG Securities EMEA plc, Morgan Stanley & Co. International Plc, and Nomura International Plc. These PRA-designated investment firms publish annual audited financial statements. *See, e.g.,* Barclays Capital Securities Limited 2020 Annual Report, available at: *https://find-and-update.company-information.service.gov.uk/company/01929333/filing-history*; Citigroup Global Markets Limited 2019 Annual Report, available at: *https://find-and-update.company-information.service.gov.uk/company/01763297/filing-history*; Credit Suisse Securities (Europe) Limited Annual Report 2020, available at: *https://www.credit-suisse.com/ch/en/investment-banking/financial-regulatory/european-financials.html*; Goldman Sachs International Annual Report 2020, available at: *https://www.goldmansachs.com/investor-relations/financials/current/subsidiary-financial-info/gsi/12–31–20-financial-statements.pdf*; Merrill Lynch International 2020 Annual Report, available at: *https://d1io3yog0oux5.cloudfront.net/_9d85f1cf3d21160d5542784492310fed/bankofamerica/db/914/9397/pdf/Merrill+Lynch+International+2020+Financial+Statements.pdf*; MUFG Securities EMEA plc 2020 Annual Report, available at: *https://www.mufgemea.com/images/mufg/MUS_EMEA_Financial_Statement_2020.pdf*; Morgan Stanley & Co. International Plc 2020 Annual Report, available at: *https://www.morganstanley.com/about-us-ir/pdf/MSIP_Group_Accounts_31_December_2020.pdf*; and Nomura International Plc 2020 Annual Report, available at: *https://find-and-update.company-information.service.gov.uk/company/01550505/filing-history.*

[245] *See* SIFMA 5/3/2021 Letter at 10–11, Appendix C. The categories of liquid assets identified in the Balance Sheet Table are: (1) ''Cash/Cash Equivalents; (2) ''Collateralised Agreements;'' (3) ''Trade/Other Receivables; cash collateral pledged;'' and (4) ''Trading/Financial Assets.'' SIFMA 5/3/2021 Letter Appendix C.

[246] *See* para. (c)(1)(iii)(B)(*1*) of the Order.

[247] *See, e.g.,* International Financial Reporting Standards Foundation (''IFRS''), *IAS 7 Statement of Cash Flows* (defining ''cash'' as comprising cash on hand and demand deposits and ''cash equivalents'' as short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value). *See also* Books and Records Adopting Release, 84 FR at 68673–74 (the section of the amended Part II of the FOCUS Report setting forth the assets side of the balance sheet and identifying cash as an allowable asset in Box 200).

[248] *See* para. (c)(1)(iii)(B)(*2*) of the Order.

[249] *See* Books and Records Adopting Release, 84 FR at 68673–74 (the section of the amended Part II of the FOCUS Report setting forth the assets side of the balance sheet and identifying securities borrowed as an allowable asset in Boxes 240 and 250 and securities purchased under agreements to resell as an allowable asset in Box 360).

[250] *See* para. (c)(1)(iii)(B)(*3*) of the Order.

[251] *See* Books and Records Adopting Release, 84 FR at 68673–74 (the section of the amended Part II of the FOCUS Report setting forth the assets side of the balance sheet and identifying fails to deliver as allowable assets in Boxes 220 and 230, receivables from clearing organizations as allowable assets in Boxes 280 and 290, and receivables from customers as allowable assets in Boxes 310, 320, and 330).

[252] *See* para. (c)(1)(iii)(B)(*4*) of the Order.

[253] *See* Books and Records Adopting Release, 84 FR at 68673–74 (the section of the amended Part II of the FOCUS Report setting forth the assets side of the balance sheet and identifying securities, commodities, and swaps positions as allowable assets in Box 12019).

[254] *See* Better Markets Letter at 7; Americans for Financial Reform Education Fund Letter at 2. *See also* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18387 (discussing the different treatment of initial margin posted to a counterparty).

lender.[255] As discussed above, one critical difference between Exchange Act rule 18a–1 and the Basel capital standard is that an SBS Entity cannot count as capital the amount of initial margin posted to a counterparty or third-party custodian unless it enters into a special loan agreement with an affiliate.[256] Under the Basel capital standard, a Covered Entity can count initial margin posted away as capital without the need to enter into a special loan arrangement with an affiliate. Consequently, to count initial margin posted away as a liquid asset for purposes of the second additional capital condition, the Covered Entity must enter into the same type of special agreement that an SBS Entity must execute to count initial margin as an allowable asset for purposes of Exchange Act rule 18a–1.[257]

If an asset does not fall within one of the five categories of ''liquid assets'' as defined in the Order,[258] it will be considered non-liquid, and could not be treated as a liquid asset for purposes of the second additional capital condition in the Order. For example, one commenter listed the following categories of non-liquid assets on the Balance Sheet Table: (1) ''Investments;'' (2) ''Loans;'' and (3) ''Other Assets.'' [259] These categories of assets generally could not be treated as liquid asset. The non-liquid ''investment'' category would include the Covered Entity's ownership interests in subsidiaries or other affiliates. The non-liquid ''loans'' category would include unsecured loans and advances. The non-liquid ''other'' assets category refers to assets that do not fall into any of the other categories of liquid or non-liquid assets. These non-liquid ''other'' assets would include furniture, fixtures, equipment, real estate, property, leasehold improvements, deferred tax assets, prepayments, and intangible assets.

As discussed above, the first prong of the second additional capital condition will require the Covered Entity to subtract total liabilities from total liquid assets and then apply a deduction (haircut) to the difference.[260] The amount remaining after the deduction will need to equal or exceed $20 million. The method of calculating the amount of the deduction relies on the calculations Covered Entities must make under the Basel capital standard.[261] In particular, under the Basel capital standard, Covered Entities must risk-weight their assets. This involves adjusting the nominal value of each asset based on the inherent risk of the asset. Less risky assets are adjusted to lower values (*i.e.,* have less weight) than more risky assets. As a result, Covered Entities must hold lower levels of regulatory capital for less risky assets and higher levels of capital for riskier assets. Similarly, under Exchange Act rule 18a–1, less risky assets incur lower haircuts than riskier assets and, therefore, require less net capital to be held in relation to them. Consequently, the process of risk-weighting assets under the Basel capital standard provides a method to account for the inherent risk in an asset held by a Covered Entity similar to how the haircuts under the Exchange Act rule 18a–1 account for the risk of assets held by SBS Entities. For these reasons, it is appropriate to use the process of risk-weighting assets under the Basel capital standard to determine the amount of the deduction (haircuts) under the first prong of the second additional capital condition.

Under the Basel capital standard, Covered Entities must hold regulatory capital equal to at least 8% of the amount of their risk-weighted assets.[262] Therefore, the deduction (haircut) required for purposes of the first prong of the second additional capital condition is determined by dividing the amount of the Covered Entity's risk-weighted assets by 12.5 (*i.e.,* the reciprocal of 8%).[263] In sum, the Covered Entity must maintain an excess of liquid assets over total liabilities that equals or exceeds $100 million before the deduction (derived from the firm's risk-weighted assets) and $20 million after the deduction.[264]

The second prong of the second additional capital condition requires the Covered Entity to make and preserve for three years a quarterly record that: (1) Identifies and values the liquid assets maintained pursuant to the first prong; (2) compares the amount of the aggregate value the liquid assets maintained pursuant to the first prong to the amount of the Covered Entity's total liabilities and shows the amount of the difference between the two amounts (''the excess liquid assets amount''); and (3) shows the amount of the deduction required under the first prong and the amount that deduction reduces the excess liquid assets amount.[265] This prong has been modified from the proposed Order to conform to the modifications to the first and third prongs of the proposed capital condition discussed above (*i.e.,* combining them into a single prong that imposes a simplified net liquid assets test). Under the Order, the quarterly record will include details showing whether the Covered Entity is meeting the $100 million and $20 million requirements of the first prong.

The third prong of the second additional capital condition requires the Covered Entity to notify the Commission in writing within 24 hours in the manner specified on the Commission's website if the Covered Entity fails to meet the requirements of the first prong and include in the notice the contact information of an individual who can provide further information about the failure to meet the requirements.[266] As discussed above, the first additional capital condition requires the Covered Entity to apply substituted compliance with respect to notification requirements of Exchange Act rule 18a–8 relating to capital.[267] A Covered Entity applying substituted compliance with respect to Exchange

[255] *See* para. (c)(1)(iii)(B)(*5*) of the Order.

[256] *See* Capital and Margin Adopting Release, 84 FR at 43887–88.

[257] *See* Capital and Margin Adopting Release, 84 FR at 43887–88.

[258] *See* para. (c)(1)(iii)(B) of the Order.

[259] *See* SIFMA 5/3/2021 Letter Appendix C.

[260] *See* para. (c)(1)(ii)(A)(*1*) of the Order.

[261] *See* BCBS, *Risk-based capital requirements (RBC20),* available at: *https://www.bis.org/basel_framework/chapter/RBC/20.htm?inforce=20191215&published=20191215.*

[262] *See* BCBS, *Risk-based capital requirements (RBC20).*

[263] *See* para. (c)(1)(iii)(C) of the Order. The Commission acknowledges that a Covered Entity's risk-weighted assets will include components in addition to market and credit risk charges (*e.g.,* operational risk charges). However, the Commission expects the combined market and credit risk charges will make up the substantial majority of the risk-weighted assets. In addition, the Commission believes that this method of calculating the deduction in the first prong of the second additional capital condition is a reasonable approach in that it addresses market and credit risk similar to the process used by security-based swap dealers authorized to use internal models to compute market and credit risk deductions under Exchange Act rule 18a–1. *See, e.g.,* Exchange Act rule 18a–1(e) (prescribing requirements to calculate market and credit risk charges, including use of an 8% multiplication factor for calculating the credit risk charges).

[264] For example, assume a Covered Entity has total assets of $600 million (of which $595 million are liquid and $5 million are illiquid) and total liabilities of $450 million. In this case, the Covered Entity's liquid assets would exceed total liabilities by $145 million ($590 million minus $450 million) and, therefore, the Covered Entity would have excess liquid assets greater than $100 million as required by the first prong of the second additional capital condition. Assume further that the Covered Entity's risk-weighted assets under the Basel capital standard equal $400 million. In this case, the Covered Entity's deduction would equal $32 million ($400 million divided by 12.5). Subtracting $32 million from $145 million leaves $113 million, which exceeds $20 million. Therefore, the Covered Entity would meet the second requirement of the first prong of the second additional capital condition.

[265] *See* para. (c)(1)(iii)(A)(*2*) of the Order.

[266] *See* para. (c)(1)(iii)(A)(*3*) of the Order.

[267] *See* para. (c)(1)(ii) of the Order.

Act rule 18a–8 must simultaneously submit to the Commission any notifications relating to capital that it must submit to the UK authorities. However, UK notification requirements do not address a failure to adhere to the simplified net liquid assets test required by the first prong of the second additional capital condition. Moreover, due to the differences between Exchange Act rule 18a–1 and the Basel capital standard discussed above, a Covered Entity could fall out of compliance with the requirements of the first prong but still remain in compliance with the requirements of the Basel capital standard. Accordingly, the third prong requires the Covered Entity to notify the Commission if the firm fails to meet the requirements of the first prong. This will alert the Commission of potential issues with the Covered Entity's financial condition that could pose risks to the firm's customers and counterparties.

The fourth prong of the additional capital condition in the proposed Order would have required the Covered Entity to include its most recently filed statement of financial condition (whether audited or unaudited) with its initial notice to the Commission of its intent to rely on substituted compliance. No commenters raised specific concerns with this condition and the Order includes it as proposed, but now it is the fourth prong of the *second* additional capital condition.[268]

The commenter who opposed additional capital conditions stated that their burdens would be disruptive to market participants and could cause Covered Entities to exit the U.S. security-based swap market.[269] However, as discussed below, based on other comments and staff analysis of the balance sheets of the PRA-designated firms, this may not be case. For example, the commenter stated that the Covered Entities expected to register with the Commission transact predominantly in securities and derivatives and do not extensively engage in unsecured lending or other activities more typical of banks.[270] The commenter based this statement on a high-level review of public information about the balance sheets of six Covered Entities undertaken to create the Balance Sheet Table.[271] Based on this review, the commenter stated that the ''vast majority of each firm's total assets consists of cash and cash equivalents, collateralized agreements, trade and other receivables, and other trading and financial assets. The commenter characterized these assets as being ''liquid.'' The commenter stated further that the amount of illiquid assets held by these firms as a proportion of their balance sheets is comparable to the proportion of illiquid assets held by U.S. broker-dealers. The commenter also stated that the long-term debt, subordinated debt, and equity of the Covered Entities, as a proportion of their total liabilities and equity, also was comparable to U.S. broker-dealers. Moreover, based on the Balance Sheet Table and the staff's analysis of the public financial reports of the PRA-designated investment firms, these firms report total liquid assets that exceed total liabilities and, in most cases, substantially in excess of $100 million.

This information suggests that Covered Entities may be able to meet the second additional capital condition without having to significantly adjust their assets, liabilities, and equity. Moreover, the modifications to the second additional capital condition that incorporate how Covered Entities categorize liquid and illiquid assets and calculate risk-weighted assets, will allow them to use existing processes to derive the measures needed to adhere to the condition. Therefore, while the condition imposes a simplified net liquid assets test and associated recordkeeping requirement, it may not cause Covered Entities to withdraw from the U.S. security-based swap market. Nonetheless, it is possible that the simplified net liquid assets test and associated recordkeeping burden could cause a Covered Entity to withdraw from the U.S. security-based swap market. However, as discussed above, this additional capital condition is designed to produce a comparable regulatory outcome with respect to SBS Entities subject to Exchange Act rule 18a–1 and Covered Entities applying substituted compliance with respect to that rule.

In response to a specific request for comment in the proposed Order, a commenter stated that the capital conditions would not be necessary if the balance sheets of the Covered Entities seeking to apply substituted compliance with respect to Exchange Act rule 18a–1 were similar to the balance sheets of U.S. broker-dealers.[272] However, the Commission also sought comment on whether the capital conditions would serve to ensure that these firms do not engage in non-securities business activities that could impair their liquidity.[273] Two commenters expressed support for the capital conditions.[274] The fact that today certain Covered Entities have liquid balance sheets does not mean this will hold true in the future or with respect to other potential registrants. For these reasons, it is appropriate to include the additional capital condition with respect to applying substituted compliance to Exchange Act rule 18a–1.

It would not be appropriate to take a more incremental approach to the additional capital conditions as suggested by a commenter.[275] Substituted compliance is premised on comparable regulatory outcomes. As discussed above, the additional capital condition is designed to supplement the UK capital laws in order to achieve a comparable regulatory outcome in terms of the net liquid assets test of Exchange Act rule 18a–1. Delaying the implementation of the additional capital condition would mean that Covered Entities are operating as registered security-based swap dealers under a capital standard that does impose the net liquid assets test. This would be inconsistent with the objective of substituted compliance and could increase risk to the U.S. security-based swap markets and participants in those markets. Moreover, the modifications to the capital condition discussed above may ease the implementation burdens.

In addition, the Commission does not believe a commenter's suggestion for an alternative capital condition requiring a Covered Entity to maintain $100 million of HQLA as defined in the LCR requirements would be adequate in terms of achieving comparable regulatory outcomes with Exchange Act rule 18a–1.[276] The Balance Sheet Table indicates that Covered Entities have total liabilities of many billions of dollars.[277] A condition requiring $100 million in HQLA would not cover these liabilities and would not impose a net liquid assets test.

Finally, the Commission has modified the citations to UK laws in the capital

[268] *See* para. (c)(1)(iii)(A)(*4*) of the Order. As discussed above, a commenter objected to the capital conditions generally and provided specific comments with respect to the first three conditions, but not the fourth condition. *See* SIFMA 5/3/2021 Letter at 9–20. This commenter did support the fourth condition as part of its recommended incremental approach to implementing the capital conditions. *See* SIFMA 5/3/2021 Letter at 19–20.

[269] *See* SIFMA 5/3/2021 Letter at 19.

[270] SIFMA 5/3/2021 Letter at 10–11.

[271] *See* SIFMA 5/3/2021 Letter at 10–11, Appendix C.

[272] *See* SIFMA 5/3/2021 Letter at 10; UK Substituted Compliance Notice and Proposed Order, 86 FR at 18407.

[273] UK Substituted Compliance Notice and Proposed Order, 86 FR at 18407.

[274] *See* Better Markets Letter at 7; Americans for Financial Reform Education Fund Letter at 1–2.

[275] *See* SIFMA 5/3/2021 Letter at 19–20.

[276] *See* SIFMA 5/3/2021 Letter at 19–20.

[277] *See* SIFMA 5/3/2021 Letter at Appendix C.

section of the Order in response to comment and further analysis.[278] In response to comments, the capital section of the Order does not cite ''recitals'' because they are not part of a legally binding regulation.[279] A commenter recommended that citations to FCA IFPRU and BIPRU rules be deleted since it is likely that only PRA-designated investment firms will rely on the substituted compliance determination for capital.[280] The FCA similarly indicated that the only firms that will rely on a substituted compliance determination for capital are PRA-designated investment firms. PRA-designated firms are not subject to FCA IFPRU and BIPRU firm requirements.[281] Further, investment firms that are not PRA-designated (*i.e.,* that are MiFID investment firms prudentially regulated by the FCA in the UK) will be subject in the near term to a new capital regime that is not based on the Basel Capital Standard, and is not addressed by the FCA's comparability analysis for capital in the FCA Application.[282]

A commenter recommended that the citations to FCA PRIN and CASS be deleted.[283] The Commission agrees it is appropriate to delete references to FCA PRIN since the entities relying on substituted compliance for capital in the UK will be PRA-designated investment firms. These firms are subject to the PRA Fundamental Rules. Therefore the Commission is deleting the references to FCA PRIN in the Order and replacing them with references to PRA Fundamental Rules 2.3 and 2.4. These rules require that firms must at all times maintain adequate financial resources, and have effective risk strategies and risk management systems. Further, the Commission also agrees that it is appropriate to delete references to FCA CASS in the Order because they relate to customer protection requirements, and not capital requirements, and Covered Entities also are subject to the Commission's segregation requirements under Exchange Act rule 18a–4,[284] as well as the segregation provisions under the UK EMIR Margin RTS.[285] Substituted compliance is not available for segregation requirements under Exchange Act rule 18a–4.[286]

In addition, in response to a recommendation to delete references to the UK EMIR margin requirements, the Commission is retaining the references to the UK Margin RTS requirements as the UK Application states ''if liquidation did occur, UK regulations also protect counterparties and promote continued market liquidity through margin requirements.''[287] The Commission agrees with the commenter that the scope of the PRA Notifications Rule is overly broad and, in response, is narrowing the references to those citations included in the comparability analysis of Exchange Act rule 18a–8.[288] Further, the Commission agrees with the commenter that some of the citations do not relate to requirements imposed on Covered Entities, but generally relate to the powers of relevant authorities. In these cases, citations in the ordering language have been deleted or modified to reference requirements that a Covered Entity is subject to and must comply with.[289]

The Commission agrees with the comments that the specific provisions to the UK CRR cited in the proposed Order are not comprehensive.[290] In response, the Commission has modified the final ordering language to use more comprehensive citations to the UK CRR (including the specific UK CRR provisions cited in the proposed Order), as the capital analysis includes only discussion of entities that are fully subject to UK CRR and CRD IV.[291] In addition, this commenter recommended that the Commission modify the final ordering language to qualify the citations to the UK CRR with a reference to waivers and permissions.[292] In response, the specific provisions in the UK CRR referenced in the capital comparability analysis were analysed without reference to waivers or permissions, and the condition states that the Covered Entity must be subject to and comply with these specific capital requirements. Therefore, the more comprehensive references to the UK CRR in the final order are cited without reference to waivers or permissions. Finally, the references to the UK CRR and the final references in the capital ordering language contribute to the conclusion that UK law produces a comparable regulatory outcome to the capital requirements under the Exchange Act.

2. Margin

The Commission's preliminary view, based on the FCA Application and the Commission's review of applicable UK laws, was that relevant UK margin requirements would produce regulatory outcomes that are comparable to those associated with Exchange Act margin requirements without the need for additional conditions.[293] For example, in adopting final margin requirements for non-cleared security-based swaps, the Commission modified the rule to more closely align it with the margin rules of the Commodity Futures Trading Commission and the U.S. prudential regulators and, in doing so, with the recommendations made by the BCBS and the Board of the International Organization of Securities Commissions (''IOSCO'') with respect to margin requirements for non–centrally cleared derivatives.[294]

Exchange Act rule 18a–3 and the UK margin rules require firms to collect liquid collateral from a counterparty to cover variation and/or initial margin requirements.[295] Both sets of rules also require firms to deliver liquid collateral to a counterparty to cover variation margin requirements. Under both sets of rules, the fair market value of collateral used to meet a margin requirement must be reduced by a haircut.[296] Further, both

[278] SIFMA 5/3/2021 Letter at 10–11, Appendix A.

[279] *See* Better Markets Letter at 5–6.

[280] SIFMA 5/3/2021 Letter at Appendix A.

[281] *See* SIFMA 5/3/2021 Letter at Appendix A.

[282] FCA Application Annex V (Side Letter for Capital Requirements) at 367 (''For the purposes of this application, we address the currently applicable UK Capital Framework—*i.e.,* based on CRR (as amended by the currently effective elements of CRR II) and CRD IV.4.'').

[283] *See* SIFMA 5/3/2021 Letter Appendix A.

[284] 17 CFR 240.18a–4.

[285] The Commission also is retaining the references to the UK EMIR Margin RTS in the final order as part of the capital condition. These standards require a Covered Entity to segregate initial margin from the firm's assets by either placing it with a third-party holder or custodian or via other legally binding arrangements, making the initial margin remote in the case of the firm's default or insolvency. FCA Application Annex V (Side Letter for Capital Requirements) at 369.

[286] *See* Capital and Margin Adopting Release, 84 FR at 43950–51.

[287] FCA Application Annex V (Side Letter for Capital Requirements) at 378.

[288] 17 CFR 240.18a–8. Therefore, the references to the PRA Notifications Rule will be modified in the final order to read PRA Notifications Rule 2.1, 2.4 through 2.6, 2.8, 2.9.

[289] More specifically, in the final order, the Commission is deleting references to the Banking Act of 2009, Capital Requirements Regulations 2013, Capital Requirements (Capital Buffers and Macro-prudential Measures) Regulations 2014, Part 8 of the Bank Recovery and Resolution (No 2) Order 2014, Bank of England Act 1998 (Macro-prudential Measures) (No 2) Order 2015, and Parts 4A and 12A of FSMA.

[290] *See* SIFMA 5/3/2021 Letter Appendix A.

[291] *See* FCA Application Annex V (Side Letter for Capital Requirements) at 366, n.400. More specifically, in the final order, the Commission is including references to the UK CRR to read: UK CRR, Part One (General Provisions) Article 6(1), Part Two (Own Funds), Part Three (Capital Requirements), Part Four (Large Exposures), Part Five (Exposures to Transferred Credit Risk), Part Six (Liquidity), and Part Seven (Leverage).

[292] *See* SIFMA 5/3/2021 Letter Appendix A.

[293] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18386.

[294] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18386, n.82.

[295] *See* 17 CFR 240.18a–3(c)(1)(ii) and FCA Application at 32–35.

[296] *See* 17 CFR 240.18a–3(c)(1)(ii) and FCA Application at 40–43.

sets rules permit the use of a model (including a third party model such as ISDA's SIMM™ model) to calculate initial margin.[297] The initial margin model under both sets of rules must meet certain minimum qualitative and quantitative requirements, including that the model must use a 99 percent, one-tailed confidence level with price changes equivalent to a 10-day movement in rates and prices.[298] Both sets of rules have common exceptions to the requirements to collect and/or post initial or variation margin, including exceptions for certain commercial end users, the Bank for International Settlements, and certain multilateral development banks.[299] Both sets of rules also permit a threshold below which initial margin is not required to be collected and incorporate a minimum transfer amount.[300]

In the UK Substituted Compliance Notice and Proposed Order, the Commission stated substituted compliance with respect to the margin requirements accordingly would be conditioned on Covered Entities being subject to those UK provisions that, the Commission has determined, in the aggregate, establish a framework that produces outcomes comparable to those associated with the requirements under the Exchange Act rule 18a–3.[301] A commenter supported the proposed Order to grant substituted compliance in connection with margin requirements for Covered Entities, subject to technical comments with respect to refining the UK laws cited in the UK Order.[302] In particular, this commenter recommended that the citations to the UK CRR, FCA IFPRU 2.2.18R, FCA SYSC 4.1.1R, and PRA Internal Capital Adequacy Assessment Rule 4.2 be deleted from the final order, and that the Commission narrow the scope of the reference to UK EMIR article 11 to article 11(3).[303]

The Commission disagrees with the commenter that the scope of the citation to UK EMIR article 11 should be narrowed. Other provisions of UK EMIR article 11 relate to margin requirements, including the provisions regarding intragroup transactions. Therefore, the Commission is not modifying this citation in the final order. Further, the Commission agrees with the commenter that it is appropriate to delete the citations to FCA IFPRU 2.2.18R and FCA SYSC 4.1.1R from the final order since it is likely that only PRA-designated investment firms will rely on the substituted compliance determination for margin. These firms are not subject to FCA IFPRU requirements, and are subject to general organizational requirements in the PRA rulebook that were already included in the proposed Order.[304] With respect to the remaining suggestions by the commenter to delete references to the UK CRR requirements and PRA Internal Capital Adequacy Assessment Rule 4.2, the Commission concludes that these requirements which were set out in the proposed Order, contribute to the conclusion that UK law produces a comparable regulatory outcome to the margin requirements under the Exchange Act.[305] For the foregoing reasons, the first margin condition requires the covered entity to be subject to and comply with certain identified UK margin requirements.[306]

The proposed Order did not contain any additional conditions for substituted compliance with respect to the margin requirements of Exchange Act section 15F(e) and Exchange Act rule 18a–3. The Commission, however, requested comment on whether there were any conditions that should be applied to substituted compliance for the margin requirements to promote comparable regulatory outcomes.[307] As discussed below, in response to comments received, the Order includes two additional margin conditions designed to produce comparable regulatory outcomes with respect to collecting variation and initial margin from counterparties.[308]

In particular, a commenter raised general concerns with the Commission's regulatory outcomes approach to substituted compliance, and suggested additional general principles that the Commission should consider in evaluating applications for substituted compliance.[309] This commenter believed regulatory arbitrage within and outside the United States was one of the key factors that led to and exacerbated the 2008 financial crisis, and stated that the Dodd-Frank Act was enacted in response, which includes the Commission's authority to promulgate capital, margin, and other rules for non-cleared security-based swaps ''to reduce the possibility and severity of another crisis related to excessive buildup of risk in the swaps markets.'' [310]

The Commission responds to the comments on the Commission's approach to substituted compliance in part II.C.1 above. However, as stated above, the commenter raises concerns about regulatory arbitrage and the potential impacts of differences in requirements that merit re-consideration of whether additional margin conditions are needed to produce comparable regulatory outcomes.[311] When proposing margin requirements for non-cleared security-based swaps, the Commission stated that the ''Dodd-Frank Act seeks to address the risk of uncollateralized credit risk exposure arising from OTC derivatives by, among other things, mandating margin requirements for non-cleared security-based swaps and swaps.'' [312] Further, the comparability criteria for margin requirements under Exchange Act rule 3a71–6 provides that prior to making a substituted compliance determination, the Commission intends to consider (in addition to any conditions imposed) whether the foreign financial regulatory system requires registrants to adequately cover their current and future exposure to OTC derivatives counterparties, and ensures registrants' safety and soundness, in a manner comparable to the applicable provisions arising under the Exchange Act and its rules and

[297] *See* 17 CFR 240.18a–3(d)(2)(i) and FCA Application at 21.

[298] *See* 17 CFR 240.18a–3(d)(2)(i) and FCA Application at 23–27. The Commission must approve the use of an initial margin model. 17 CFR 240.18a–3(d)(2)(i). UK EMIR article 11(15) directs European supervisory authorities to develop regulatory technical standards under which initial margin models have to be approved (initial and ongoing approval). UK requirements currently provide that, upon request, counterparties using an initial margin model shall provide the regulators with any documentation relating to the risk management procedures relating to such model at any time. UK EMIR Margin RTS article 2(6).

[299] *See* 17 CFR 240.18a–3(c)(1)(iii) and FCA Application at 52–60.

[300] *See* 17 CFR 240.18a–3(c)(1)(iii) and FCA Application at 52–60.

[301] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18386.

[302] *See* SIFMA 5/3/2021 Letter at 10, Appendix A.

[303] *See* SIFMA 5/3/2021 Letter Appendix A.

[304] *See* PRA General Organisational Requirements Rule 2.1.

[305] The references to the UK CRR and PRA Internal Capital Adequacy Assessment Rule 4.2 were included in the comparability assessment for margin requirements, and in the Commission's view the holistic approach for comparing regulatory outcomes should seek to reflect the whole of a jurisdiction's relevant requirements, rather than select subsets of those requirements.

[306] *See* para. (c)(2)(i) of the Order. The first margin condition requires that Covered Entities must be subject to and comply with UK EMIR article 11; UK EMIR Margin RTS; UK CRR articles 103, 105(3); 105(10); 111(2), 224, 285, 286, 286(7), 290, 295, 296(2)(b), 297(1), 297(3), and 298(1); UK MiFID Org Reg article 23(1); PRA General Organisational Requirements Rule 2.1; and PRA Internal Capital Adequacy Assessment Rule 4.2.

[307] French Substituted Compliance Notice and Proposed Order, 85 FR at 85737.

[308] *See* paras. (c)(2)(ii) and (iii) of the Order.

[309] *See* Better Markets Letter at 3.

[310] *See* Better Markets Letter at 2.

[311] *See* Better Markets Letter at 2–3.

[312] *See* Capital, Margin, and Segregation Requirements for Security-Based Swap Dealers and Major Security-Based Swap Participants and Capital Requirements for Broker-Dealers; Proposed Rule, Exchange Act Release No. 68071 (Oct. 18, 2021), 77 FR 70214, 70258 (Nov. 23, 2012).

regulations.[313] In adopting this comparability criteria for margin requirements, the Commission stated that obtaining collateral is one of the ways OTC derivatives dealers manage their credit risk exposure to OTC derivatives counterparties.[314]

To address the risk of uncollateralized exposures, Exchange Act rule 18a–3 requires SBS Entities without a prudential regulator to collect variation margin from all counterparties, including affiliates, unless an exception applies.[315] Under the UK margin requirements, there are exceptions from the variation margin requirements for certain intragroup transactions (*i.e.,* transactions between affiliates).[316] In addition, Exchange Act rule 18a–3 requires firms to collect initial margin from all counterparties, unless an exception applies.[317] This initial margin requirement under Exchange Act rule 18a–3 requires the firm to collect initial margin from a financial counterparty such as a hedge fund without regard to whether the counterparty has material exposures to non-cleared security-based swaps and uncleared swaps. In contrast, UK margin requirements do not require Covered Entities to collect initial margin from financial counterparties, if their notional exposure to non–centrally cleared derivatives does not exceed a certain threshold on a group basis.[318]

In some cases these differences may result in a Covered Entity not being adequately collateralized to cover its current or future exposure to these counterparties with respect to its OTC derivatives transactions. In addition, differences in the counterparty exceptions could potentially incentivize market participants to engage in non-cleared security-based swap transactions outside of the United States.[319] Consequently, it is appropriate to impose additional margin conditions to produce comparable regulatory outcomes in terms of counterparty exceptions between Exchange Act rule 18a–3 and the UK requirements.

The first additional condition addresses differences in the counterparty exceptions with respect to variation margin. It requires a Covered Entity to collect variation margin, as defined in the UK EMIR Margin RTS, from a counterparty with respect to a transaction in non-cleared security-based swaps, unless the counterparty would qualify for an exception under Exchange Act rule 18a–3 from the requirement to deliver variation margin to the Covered Entity.[320] This condition defines variation margin by referencing UK EMIR Margin RTS to facilitate implementation of the condition by Covered Entities. Under this condition, for example, Covered Entities would be required to collect variation margin from their affiliates, but would be permitted to comply with all other UK margin requirements, including calculation, collateral, documentation, and timing of collection requirements. The first additional condition will close the gap between the counterparty exceptions of Exchange Act rule 18a–3 and the UK margin rules with respect to variation margin.

The second additional condition addresses differences in the counterparty exceptions with respect to initial margin. It requires a Covered Entity to collect initial margin, as defined in the UK EMIR Margin RTS, from a counterparty with respect to transactions in non-cleared security-based swaps, unless the counterparty would qualify for an exception under Exchange Act rule 18a–3 from the requirement to deliver initial margin to Covered Entity.[321] The condition defines initial margin by referencing UK EMIR Margin RTS to facilitate implementation of the condition by Covered Entities. Under this condition, for example, Covered Entities would be required to collect initial margin from their certain counterparties, but would be permitted to comply with all other UK margin requirements, including calculation, collateral, documentation, and timing of collection requirements. The second additional condition will close the gap between the counterparty exceptions of Exchange Act rule 18a–3 and the UK margin rules with respect to initial margin.

Finally, for the reasons discussed above in part III.B.2.k of this release, the third additional condition is that the Covered Entity applies substituted compliance with respect to Exchange Act rules 18a–5(a)(12) (a record making requirement).[322] This record making requirement is directly linked to the margin requirements of Exchange Act rule 18a–3. The proposed Order conditioned substituted compliance with respect to this record making requirement on the Covered Entity applying substituted compliance with respect to Exchange Act rule 18a–3.[323] This additional condition is designed to provide clarity as to the Covered Entity's obligations under this record making requirement when applying substituted compliance with respect to Exchange Act rule 18a–3 pursuant this Order.

VI. Substituted Compliance for Internal Supervision, Chief Compliance Officers and Additional Exchange Act Section 15F(j) Requirements

A. Proposed Approach

The FCA Application further requested substituted compliance in connection with requirements relating to:

- Internal supervision—Diligent supervision and conflict of interest provisions that generally require SBS Entities to establish, maintain, and enforce supervisory policies and procedures that reasonably are designed to prevent violations of applicable law, and implement certain systems and procedures related to conflicts of interest.
- Chief compliance officers—Chief compliance officer provisions that generally require SBS Entities to designate individuals with the responsibility and authority to establish, administer, and review compliance policies and procedures, to resolve conflicts of interest, and to prepare and certify annual compliance reports to the Commission.
- Additional Exchange Act section 15F(j) requirements—Certain additional

[313] *See* 17 CFR 240.3a71–6(d)(5)(i) and (ii).

[314] *See* Capital and Margin Adopting Release, 84 FR at 43949 (''Obtaining collateral is one of the ways OTC derivatives dealers manage their credit risk exposure to OTC derivatives counterparties. Prior to the financial crisis, in certain circumstances, counterparties were able to enter into OTC derivatives transactions without having to deliver collateral. When ''trigger events'' occurred during the financial crisis, those counterparties faced significant liquidity strains when they were required to deliver collateral.).

[315] *See* 17 CFR 240.18a–3(c)(ii)(A)(*1*) and (*2*).

[316] *See* FCA Application at 57.

[317] *See* 17 CFR 240.18a–3(c)(ii)(B).

[318] *See* FCA Application at 20. These thresholds are being phased-in with the last initial margin threshold set at EUR 8 billion.

[319] The Commission recognizes there are also cases where the UK margin rules are more restrictive than Exchange Act rule 18a–3. UK margin rules require Covered Entities to post initial margin to covered counterparties, while the Exchange Act rule 18a–3 would permit posting but not require it. In addition, UK margin rules also require a Covered Entity to collect (and post) initial margin to financial and non-financial counterparties if their notional exposure to non-centrally cleared derivatives exceeds a certain threshold on a group basis. In contrast, Exchange Act rule 18a–3 does not require (but permits) a nonbank security-based swap dealer to collect initial margin from counterparties that are financial market intermediaries. 17 CFR 240.18a–3(c)(1)(iii)(B). The comparability analysis, however, focuses on determining whether the UK margin rules are comparable to Exchange Act rule 18a–3.

[320] *See* para. (c)(2)(ii) of the Order.

[321] *See* para. (c)(2)(iii) of the Order.

[322] *See* para. (c)(2)(iv) of the Order.

[323] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18396–98, 18416.

requirements related to information-gathering and antitrust prohibitions.[324]

Taken as a whole, those requirements generally help to advance SBS Entities' use of structures, processes, and responsible personnel reasonably designed to promote compliance with applicable law, identify and cure instances of noncompliance, and manage conflicts of interest.

In proposing to provide conditional substituted compliance in connection with this part of the FCA Application, the Commission preliminarily concluded that the relevant UK requirements in general would produce comparable regulatory outcomes by providing that UK SBS Entities have structures and processes that reasonably are designed to promote compliance with applicable law, to identify and cure instances of non-compliance, and to manage conflicts of interest.

Substituted compliance under the proposed Order was to be conditioned in part on SBS Entities being subject to and complying with specified UK provisions that in the aggregate help to produce regulatory outcomes that are comparable to those associated with those internal supervision, chief compliance officer and related requirements under the Exchange Act.[325]

Under the proposed Order, substituted compliance would be subject to certain additional conditions to help ensure the comparability of outcomes. First, substituted compliance in connection with Exchange Act internal supervision requirements (including related information gathering requirements under Exchange Act section 15F(j)(4)(A) and related conflict of interest systems and procedures requirements under Exchange Act section 15F(j)(5)) would be conditioned on the Covered Entity complying with applicable UK supervisory and compliance provisions *as if* those provisions also require the Covered Entity to comply with applicable requirements under the Exchange Act and the other applicable conditions of the Order. This condition reflects that, even with substituted compliance, Covered Entities still directly would be subject to a number of requirements under the Exchange Act and conditions to the final Order.[326] Under the proposed Order, substituted compliance for Exchange Act internal supervision requirements would not extend to internal supervision in connection with the internal risk management requirements, certain information reporting requirements or anti-trust requirements.[327]

For similar reasons, the proposed Order conditioned substituted compliance in connection with compliance report requirements on the Covered Entity at least annually providing the Commission with all compliance reports required pursuant to UK MiFID Org Reg article 22(2)(c). Those reports would be required to be in English and accompanied by a certification under penalty of law that the report is accurate and complete, and would have to address the SBS Entity's compliance with other applicable conditions to the substituted compliance order.[328]

The Commission preliminarily did not provide substituted compliance for Exchange Act antitrust provisions, based on the preliminary conclusion that allowing an alternative means of compliance would not lead to comparable regulatory outcomes.[329]

B. Commenter Views and Final Provisions

After considering commenters' recommendations regarding internal supervision, chief compliance officer and related requirements, the Commission is making positive substituted compliance determinations in connection with internal supervision (including related information gathering requirements under Exchange Act section 15F(j)(4)(A) and related conflict of interest systems and procedures requirements under Exchange Act section 15F(j)(5)) and chief compliance officer requirements.

One commenter expressed general support for the proposed approach toward substituted compliance for the risk control provisions.[330] Another commenter stated that UK requirements are not sufficiently comparable to Exchange Act requirements.[331] As discussed below, the final Order has been changed from the proposed Order in certain respects in response to comments.[332] The Commission continues to conclude that, taken as a whole, applicable requirements under UK law require that SBS Entities have structures and processes that reasonably are designed to promote compliance with applicable law, to identify and cure instances of non-compliance, and to manage conflicts of interest, and thus produce regulatory outcomes that are comparable to those associated with the above-described internal supervision and chief compliance officer requirements. Although there are differences between the approaches taken by the relevant internal supervision and chief compliance officer requirements under the Exchange Act and relevant UK requirements, the Commission continues to believe that

[324] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18389. Section 15F(j)(4)(A) requires firms to have systems and procedures to obtain necessary information to perform functions required under section 15F. Section 15F(j)(6) prohibits firms from adopting any process or taking any action that results in any unreasonable restraint of trade, or to impose any material anticompetitive burden on trading or clearing.

[325] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18389 n.109. Each of the comparable UK internal supervision and chief compliance officer requirements listed in the proposed Order applies to a uniquely defined set of UK-authorized firms. *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18390 and n.112. To assist UK firms in determining whether they are subject to these requirements, the Commission preliminarily determined that any Covered Entity that is an ''IFPRU investment firm,'' ''UK bank'' or ''UK designated investment firm,'' each as defined for purposes of UK law, would be subject to all of the required UK requirements related to internal supervision and chief compliance officer requirements and thus eligible to apply substituted compliance for internal supervision and chief compliance officer requirements. *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18390.

[326] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18390. These residual Exchange Act requirements could, for example, relate to requirements for which substituted compliance is not available, requirements for which the Order does not make a positive substituted compliance determination, security-based swap business for which the Covered Entity is unable to satisfy the conditions of the Order, and/or requirements or security-based swap business for which the Covered Entity decides not to use substituted compliance. The condition was designed to allow a Covered Entity to use their existing internal supervision and compliance frameworks to comply with the relevant Exchange Act requirements and Order conditions, rather than having to establish separate special-purpose supervision and compliance frameworks.

[327] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18389 and n.108.

[328] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18390. The condition was designed to allow a Covered Entity to leverage the compliance reports that it must produce pursuant to UK requirements, by extending those reports to address compliance with the conditions to the proposed Order.

[329] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18390.

[330] *See* SIFMA 5/3/2021 Letter at 20–21. The commenter also requested that the Commission not require a Covered Entity to be subject to and comply with some of the UK internal supervision and chief compliance officer requirements listed in the proposed Order. In addition, the commenter requested that the Commission amend the conditions to substituted compliance for chief compliance officer requirements. *See* SIFMA 5/3/2021 Letter at 20–21 and Appendix A part (d). The Commission addresses those requests in the relevant sections of this part VI below.

[331] *See* Better Markets Letter at 2. The commenter also stated that, if the Commission nevertheless makes a positive substituted compliance determination, it must at a minimum ensure that the conditions in the proposed Order ''are applied with full force and without exceptions or dilution.'' The Commission addresses that comment in the relevant sections of this part VI below.

[332] *See* para. (d) of the Order.

those differences on balance should not preclude substituted compliance for these requirements, as the relevant UK requirements taken as a whole help to produce comparable regulatory outcomes.

To help ensure the comparability of outcomes, substituted compliance for internal supervision and chief compliance officer requirements is subject to certain conditions. Substituted compliance in connection with those requirements is conditioned on the Covered Entity being subject to, and complying with, relevant UK requirements. In addition, consistent with the proposed Order, substituted compliance for internal supervision requirements (1) is conditioned on the Covered Entity complying with the relevant UK requirements as if they also require compliance with applicable Exchange Act requirements and other applicable conditions under the Order and (2) does not extend to certain specified internal supervision requirements.[333] Consistent with the proposed Order, substituted compliance in connection with chief compliance officer requirements is conditioned on the Covered Entity at least annually providing the Commission with an English-language copy of all compliance reports required pursuant to UK MiFID Org Reg article 22(2)(c). As described below, in response to comments the Commission is amending the certification of each report to better align with the certification in Exchange Act rule 15Fk–1(c)(2)(ii)(D),[334] requiring each report to address the Covered Entity's compliance with applicable Exchange Act requirements and other applicable conditions under the Order, amending the deadline by which such reports must be provided to the Commission and clarifying that all such reports together must cover the entire period that the Covered Entity's Exchange Act annual compliance report would be required to cover. A Covered Entity that is unable to comply with an applicable condition—and thus is not eligible to use substituted compliance for the Exchange Act internal supervision and/or chief compliance officer requirements related to that condition—nevertheless may use substituted compliance for another set of Exchange Act requirements addressed in the Order if it complies with the conditions to the relevant parts of the Order.

Under the Order, substituted compliance for internal supervision and chief compliance officer requirements is not subject to a condition that the Covered Entity apply substituted compliance for related recordkeeping requirements in Exchange Act rules 18a–5 and 18a–6. A Covered Entity that applies substituted compliance for internal supervision and/or chief compliance officer requirements, but does not apply substituted compliance for the related recordkeeping requirements in Exchange Act rules 18a–5 and 18a–6, will remain subject to the relevant provisions of Exchange Act rules 18a–5 and 18a–6. Those rules require the Covered Entity to make and preserve records of its compliance with Exchange Act internal supervision and chief compliance officer requirements and of its security-based swap activities required or governed by those requirements. A Covered Entity that applies substituted compliance for internal supervision and/or chief compliance officer requirements, but complies directly with related recordkeeping requirements in rules 18a–5 and 18a–6, therefore must make and preserve records of its compliance with the relevant conditions to the Order and of its security-based swap activities required or governed by those conditions and/or referenced in the relevant parts of rules 18a–5 and 18a–6.

The Commission details below its consideration of comments on the proposed Order.

1. Applicable UK Internal Supervision and Chief Compliance Officer Requirements

Exchange Act rule 15Fh–3(h) requires an SBS Entity to establish and maintain a system to supervise, and to diligently supervise, its business and the activities of its associated persons. This system must be reasonably designed to prevent violations of the provisions of applicable Federal securities laws relating to its business as an SBS Entity. The rule specifies detailed minimum requirements for this internal supervision system. Exchange Act sections 15F(j)(4)(A) and (j)(5) similarly require a registered SBS Entity to establish and enforce internal systems and procedures to obtain any necessary information to perform any regulated functions in its capacity as an SBS Entity and to implement conflict of interest systems and procedures, respectively. Exchange Act section 15F(k)[335] and Exchange Act rule 15Fk–1 require an SBS Entity to designate a chief compliance officer with specified duties, including requirements to report directly to the SBS Entity's board of directors or senior officer, review and ensure the SBS Entity's compliance with applicable Exchange Act requirements, resolve conflicts of interest that may arise, administer the policies and procedures required by the Exchange Act, and establish and follow procedures for addressing noncompliance. In addition, the chief compliance officer must submit to the Commission an annual report of the SBS Entity's assessment of the effectiveness of its policies and procedures, material changes to the policies and procedures, areas for improvement, potential changes to its compliance program, material noncompliance matters identified, and the resources for its compliance program. Exchange Act rule 15Fk–1 further provides that the compensation and removal of the chief compliance officer must require the approval of a majority of the SBS Entity's board of directors.

A commenter requested that the Commission not require a Covered Entity to be subject to and comply with certain of the UK requirements specified in the proposed Order.[336] By contrast, another commenter stated that, if the Commission makes a positive substituted compliance determination, it must at a minimum ensure that the conditions in the proposed Order ''are applied with full force and without exceptions or dilution.'' [337] The Commission details below its consideration of each of these comments.

The commenter stated that the Commission should delete from the Order the provisions of FCA IFPRU, FCA BIPRU, and FCA SYSC 19A listed in paragraphs (d)(3)(iii) and (d)(3)(vi) of the proposed Order. These provisions apply only to IFPRU investment firms, and the commenter stated that it expects only ''banks and PRA-designated investment firms'' will register as SBS Entities.[338] For the reasons described in part III.B.2.e above, the Commission is retaining the references to these provisions.

[333] *See* para. (d)(1)(iii) of the Order. In particular, the Order does not extend to internal supervision requirements under Exchange Act rule 15Fh–3(h) related to compliance with internal risk management requirements in Exchange Act rule 15F(j)(2) (which are addressed by paragraph (b)(1) of the Order in connection with internal risk management), requirements to disclose or provide information to the Commission and any relevant U.S. prudential regulator pursuant to Exchange Act sections 15F(j)(3) and (j)(4)(B) (for which substituted compliance is not available), or the anti-trust provisions of Exchange Act section 15F(j)(6) (for which the Commission is not making a positive substituted compliance determination).

[334] 17 CFR 240.15Fk–1(c)(2)(ii)(D).

[335] 15 U.S.C. 78*o*–10(k).

[336] *See* SIFMA 5/3/2021 Letter at 20–21 and Appendix A part (d)(3).

[337] *See* Better Markets Letter at 2.

[338] *See* SIFMA 5/3/2021 Letter Appendix A part (d)(3).

Similarly, the commenter stated that the Commission should delete from the Order the provisions of FSMA and FCA COND listed in paragraph (d)(3)(vii) of the proposed Order that apply to firms regulated only by the FCA, rather than to firms dually regulated by both the FCA and the PRA.[339] The commenter again stated that it expects only dually regulated ''banks and PRA-designated investment firms'' will register as SBS Entities.[340] The proposed Order would not require a Covered Entity that is a dually regulated firm to be subject to and comply with these provisions. Rather, paragraph (d)(3)(vii) of the proposed Order would require the Covered Entity to be subject to and comply with either the provisions of FSMA and FCA COND that apply to solo-regulated firms or analogous provisions that apply to dually regulated firms. Accordingly, the Commission is retaining the references to these provisions.

The commenter also recommended that the Commission delete from the Order the following provisions because they do not correspond to and go beyond Exchange Act internal supervision and chief compliance officer requirements: [341]

- FCA CASS 6.2.1R and 7.12.1R, which implement MiFID articles 16(8) and (9), require a Covered Entity to make adequate arrangements to safeguard client assets and client money held by the Covered Entity and to prevent the use of client assets or client money for the Covered Entity's own account. FCA CASS 7.11.1R, which implements MiFID article 16(10), prohibits a Covered Entity from entering into, as part of its implementation of organizational arrangements, arrangements for a retail client to transfer full ownership of money to the Covered Entity as collateral for the client's obligations to the Covered Entity.
- PRA Internal Capital Adequacy Assessment Rules 4.1 through 4.4, 5.1, 6.1, 7.1, 7.2, 8.1 through 8.5, 9.1, 10.1, 10.2, and 11.1 through 11.3 and PRA Internal Liquidity Adequacy Assessment Rules 3.1 through 3.3, 4.1, 7.2, 8.1, 9.2, 11.1, 11.2, 11.4, 12.1, 12.3, and 12.4, which implement CRD articles 79 through 87, are described in part IV.B.1.
- FCA SYSC 4.1.1R(1), 4.1.2R, 7.1.4R, 7.1.17R, 7.1.18R, 7.1.18BR, 7.1.19R, 7.1.20R, 7.1.21R, 7.1.22R, and 19D.2.1R, PRA Remuneration Rule 6.2, and PRA Risk Control Rules 2.3, 2.7, and 3.1 through 3.5, which implement parts of CRD articles 74 and 76, are described in part IV.B.1.
- FCA SYSC 4.3A.1R, which implements parts of CRD article 88(1), requires a Covered Entity to ensure that the management body defines, oversees, and is accountable for the implementation of governance arrangements that ensure effective and prudent management of the Covered Entity, including segregation of duties and prevention of conflicts of interest.
- PRA Senior Management Functions Rule 8.2, which implements CRD article 88(1)(e), requires a Covered Entity to ensure that the same person does not serve as both the chair of the Covered Entity's governing body and the Covered Entity's chief executive officer.[342]
- FCA SYSC 4.3A.3R, which implements parts of CRD article 91(1), (2), (7), and (8), requires members of a Covered Entity's management body to have certain qualifications to be able to perform their duties, understand the Covered Entity's activities and main risks, effectively assess and challenge senior management decisions, and effectively oversee and monitor management decision-making.
- FCA SYSC 4.3A.4R, which implements parts of CRD article 91(9), requires a Covered Entity to devote adequate human and financial resources to the induction and training of members of the management body.
- FCA SYSC 9.1.1AR and PRA Record Keeping Rule 2.1, which implement MiFID article 16(6), require a Covered Entity to arrange to keep business records sufficient to assess its compliance with applicable UK legal requirements.
- FCA SYSC 10A.1.6R, 10A.1.8R, and 10A.1.11R, which implement MiFID article 16(7), require a Covered Entity to take all reasonable steps to make and keep records of telephone and electronic communications and to notify clients that telephone communications will be recorded.
- FCA SYSC 19D.3.1R, 19D.3.3R, 19D.3.7R through 19D.3.11R, 19D.3.15R, 19D.3.17R, and 19D.3.37R and PRA Remuneration Rules 3.1, 4.2, 5.1, 6.2, 8.2, and 15.2, which implement parts of CRD article 92, address implementation of a Covered Entity's remuneration policy in a manner that avoids conflicts of interest and that is consistent with sound and effective risk management, as well as internal supervision and review of this implementation for compliance with the policies and procedures adopted by the management body.
- PRA Fundamental Rule 5,[343] which contains provisions similar to MiFID articles 16(4) and (5), requires a Covered Entity to have effective risk strategies and risk management systems.
- UK CRR articles 286 through 288 and 293 [344] are described in part IV.B.1.
- UK EMIR Margin RTS article 2 [345] is described in part IV.B.1.
- UK MiFID Org Reg articles 23,[346] 27, 30 through 32, 35, 36, and 72 through 76 and Annex IV address a Covered Entity's policies and procedures governing risk management, remuneration, and documentation of compliance, the Covered Entity's supervision of and responsibility for outsourced functions and documentation of conflicts of interest relevant to the Covered Entity's compliance with conflict of interest requirements.

Taken as a whole, these UK requirements help to produce regulatory outcomes comparable to Exchange Act requirements to establish internal systems to supervise the Covered Entity's business and associated persons, obtain information necessary to perform regulated functions in its capacity as an SBS Entity and address conflicts of interest, as well as Exchange Act requirements to submit an annual compliance report to the Commission and to ensure that the chief compliance officer's removal and compensation is subject to approval by a majority of the board of directors. The comparability analysis requires consideration of Exchange Act requirements as a whole against analogous UK requirements as a whole, recognizing that U.S. and non-U.S. regimes may follow materially different approaches in terms of specificity and technical content. This ''as a whole'' approach—which the Commission is following in lieu of requiring requirement-by-requirement

[339] *See* SIFMA 5/3/2021 Letter Appendix A part (d)(3).

[340] *See* SIFMA 5/3/2021 Letter Appendix A part (d)(3).

[341] *See* SIFMA 5/3/2021 Letter Appendix A part (d)(3).

[342] To ensure that Covered Entities regulated only by the FCA and not the PRA must be subject to and comply with a similar requirement, the Commission is adding FCA SYSC 4.3A.2R to the list of UK requirements in paragraph (d)(3) of the Order.

[343] The commenter stated that these requirements are more appropriately addressed in connection with substituted compliance for internal risk management requirements. As discussed below, the Commission believes that these UK requirements are relevant to substituted compliance for Exchange Act internal supervision and chief compliance officer requirements.

[344] The commenter also stated that these requirements are more appropriately addressed in connection with substituted compliance for capital and margin requirements. *See* SIFMA 5/3/2021 Letter Appendix A part (d)(3). As discussed below, the Commission believes that these UK requirements are relevant to substituted compliance for Exchange Act internal supervision and chief compliance officer requirements.

[345] *See supra* note 344.

[346] *See supra* note 343.

similarity—further means that the conditions to substituted compliance should encompass all UK requirements that establish comparability with the applicable regulatory outcome, and helps to avoid ambiguity in the application of substituted compliance. It would be inconsistent with the holistic approach to excise relevant requirements and leave only the residual UK provisions that most closely resemble the analogous Exchange Act requirements.[347] Moreover, because Exchange Act internal supervision and chief compliance officer requirements serve the purpose of causing SBS Entities to have systems and follow practices to help ensure they conduct their businesses as required, it would be paradoxical to conclude that an SBS Entity that fails to implement requisite internal risk management, documentation, capital, and/or margin systems and practices nonetheless may be considered to be following internal supervision and chief compliance officer standards that are sufficient to meet the regulatory outcomes required under the Exchange Act. An internal risk management, documentation, capital, or margin-related failure necessarily constitutes a compliance failure. For these reasons, the Commission believes that these UK provisions appropriately constitute part of the substituted compliance conditions for internal supervision and chief compliance officer requirements and is retaining the references to these provisions. In reaching this conclusion, the Commission emphasizes the importance of ensuring that substituted compliance is grounded on the comparability of regulatory outcomes. Retaining conditions of the Order necessary to help produce regulatory outcomes comparable to Exchange Act internal risk management requirements also should address another commenter's concern that any substituted compliance determination not weaken the internal supervision and chief compliance officer conditions in the proposed Order.[348]

The Commission is making two changes to the proposed Order's list of UK requirements to which a Covered Entity must be subject and with which it must comply if it uses substituted compliance for internal supervision and/or chief compliance officer requirements. First, the UK Substituted Compliance Notice and Proposed Order requested comment on whether the Commission should revise the Order to require compliance with UK provisions that implement CRD articles 93 to 95 which relate to a Covered Entity's remuneration policies.[349] The proposed additions were intended to promote compliance goals similar to those of the other UK requirements listed in paragraph (d)(3) of the proposed Order.[350] No commenters addressed this issue, and the Commission has determined to add a requirement for the Covered Entity to be subject to and comply with certain provisions of either FCA SYSC 19A (in the case of a Covered Entity that is an IFPRU investment firm) or FCA SYSC 19D (in the case of a Covered Entity that is a UK bank or UK designated investment firm).[351] These provisions together implement CRD articles 94 and 95 and address additional aspects of a Covered Entity's internal systems for preventing and addressing conflicts of interest related to compensation. The Commission is not adding provisions that implement CRD article 93, as they relate to remuneration policies for institutions that benefit from exceptional government intervention. The Commission believes that the UK provisions implementing CRD articles 94 and 95 are necessary to better promote regulatory outcomes comparable to the relevant Exchange Act requirements on a holistic, outcomes-oriented basis. Second, the Commission is requiring a Covered Entity using substituted compliance for internal supervision and/or chief compliance officer requirements to be subject to and comply with FCA SYSC 4.3A.2R. This requirement implements parts of CRD article 88(1) and is nearly identical to PRA Senior Management Functions Rule 8.2, which appeared in the proposed Order.[352] Including FCA SYSC 4.3A.2R will ensure that Covered Entities regulated by only the FCA, rather than by the FCA and the PRA together, will be subject to a requirement similar to PRA Senior Management Functions Rule 8.2. In deciding to make a positive substituted compliance determination for UK internal supervision and chief compliance officer requirements, the Commission considers that the Order's condition requiring a Covered Entity to be subject to and comply with all of the UK requirements listed in paragraph (d)(3) of the Order help to produce regulatory outcomes comparable to Exchange Act internal supervision and chief compliance officer requirements. The Commission recognizes that some of the UK requirements related to internal supervision and chief compliance officers follow a more granular approach than the high-level approach of Exchange Act internal supervision and chief compliance officer requirements, but these UK requirements, taken as a whole, are crafted to promote a Covered Entity's compliance with applicable law and ability to identify and cure instances of noncompliance and manage conflicts of interest. Within the requisite outcomes-oriented approach for analyzing comparability, the Commission concludes that a Covered Entity's failure to comply with any of those UK internal supervision and chief compliance officer requirements would be inconsistent with a Covered Entity's obligations under Exchange Act internal supervision and chief compliance officer requirements and that compliance with the full set of UK requirements listed in paragraph (d)(3) of the Order would promote comparable regulatory outcomes.

2. Compliance Reports

A commenter requested that the Commission amend three aspects of the proposed Order's compliance report-related condition to a Covered Entity's use of substituted compliance for chief compliance officer requirements.[353] Another commenter stated that, if the Commission makes a positive substituted compliance determination, it must at a minimum ensure that the conditions in the proposed Order ''are applied with full force and without exceptions or dilution.'' [354] The Commission details below its consideration of each of these requests.

First, the proposed Order would require all compliance reports required by UK law to include a certification that, under penalty of law, the report is accurate and complete.[355] The commenter requested that the Commission revise this certification to conform more closely with the required certification of annual compliance reports pursuant to Exchange Act rule 15Fk–1.[356] Rule 15Fk–1 requires an

[347] The Commission further believes that those conditions to substituted compliance do not expand the scope of Exchange Act requirements because substituted compliance is an option available to non-U.S. person SBS Entities—not a mandate.

[348] *See* Better Markets Letter at 2.

[349] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18409.

[350] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18409.

[351] *See* para. (d)(3)(vi) of the Order.

[352] *See supra* note 342 and accompanying text.

[353] *See* SIFMA 5/3/2021 Letter at 20–21 and Appendix A part (d)(2)(ii).

[354] *See* Better Markets Letter at 2.

[355] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 85692.

[356] *See* SIFMA 5/3/2021 Letter at 20 and Appendix A part (d)(2) (stating that paragraph (d)(2)(ii)(B) of the Order, consistent with Exchange Act rule 15Fk–1(c)(2)(ii)(D), should be amended so

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annual compliance report to include ''a certification by the chief compliance officer or senior officer that, to the best of his or her knowledge and reasonable belief and under penalty of law, the information contained in the compliance report is accurate and complete in all material respects.'' [357] The Commission concurs that the Order's required certification should align with that of Exchange Act rule 15Fk–1. It would seem incongruous and not within the intent of substituted compliance to apply a higher standard of certification to Covered Entities relying on substituted compliance than required under that rule. Therefore, the Commission is amending the Order to require that all required UK compliance reports include a certification signed by the chief compliance officer or senior officer of the Covered Entity that, to the best of the certifier's knowledge and reasonable belief and under penalty of law, the report is accurate and complete in all material respects.[358] In addition, the Order has been updated to clarify that each UK compliance report, and therefore also the chief compliance officer or senior officer certification, must address the Covered Entity's compliance with applicable Exchange Act requirements, consistent with the Order's conditions with respect to internal supervision.[359] The Commission believes that this clarification is necessary to promote comparable regulatory outcomes, particularly in light of the granular approach to substituted compliance, to ensure that the compliance report covers applicable Exchange Act requirements if the Covered Entity uses substituted compliance for chief compliance officer requirements, whether or not the Covered Entity relies on substituted compliance for internal supervision.

Second, because Covered Entities may prepare multiple UK compliance reports per year, the commenter requested that the Commission permit a Covered Entity ''to either (a) make an annual submission of these multiple reports with a supplement of information regarding compliance with conditions to substituted compliance or (b) create and submit a single, annual report regarding its SBS Entity business, including information regarding compliance with conditions to substituted compliance.'' [360] The Commission is persuaded that additional clarification regarding the timing of these UK compliance reports is warranted, but believes that submission of multiple outdated and/or subsequently superseded UK compliance reports at the end of each year likely would not promote regulatory outcomes comparable to Exchange Act compliance report requirements. Rather, in the case of a Covered Entity that prepares multiple UK compliance reports each year, the Commission believes that it is appropriate for the Commission to receive compliance reports shortly after their submission to the management body. Providing these reports to the Commission near the times that the Covered Entity submits them to the management body also will better align with the UK regulatory framework, which permits a Covered Entity to prepare and submit to the management body multiple compliance reports throughout the year, but does not contemplate a Covered Entity preparing multiple internal compliance reports throughout the year and submitting those reports to the management body only at the end of the year. The Commission thus is changing the Order to clarify that a Covered Entity must provide the Commission each UK compliance report prepared pursuant to UK MiFID Org Reg article 22(2)(c) no later than 15 days following the earlier of its submission to the Covered Entity's management body or the time the report is required to be submitted to the management body.[361] In line with UK MiFID Org Reg article 22(2)(c), a Covered Entity must provide at least one report annually to the Commission but if a Covered Entity makes more than one report pursuant to UK MiFID Org Reg article 22(2)(c), the Covered Entity must provide and certify each such report within the required 15-day deadline. The Commission views 15 days as providing a reasonable time to translate reports, if needed, and convey them to the Commission, and this change is consistent with the same commenter's suggested clarification of the French Substituted Compliance Notice and Proposed Order.[362] This deadline is intended to promote timely notice of compliance matters in a manner comparable to Exchange Act requirements, while also accounting for the annual deadline required under UK MiFID Org Reg article 22(2)(c) as well as the possibility that the Covered Entity may submit reports ahead of this annual deadline. In addition, reports required to be provided under UK MiFID Org Reg article 22(2)(c) must together cover the entire period that an Exchange Act rule 15Fk–1 annual report would have covered.[363] This requirement prevents a Covered Entity from notifying the Commission just prior to the due date of its annual Exchange Act compliance report that it will use substituted compliance for chief compliance officer requirements and then providing the Commission a UK compliance report that covers only a part of the year that would have been covered in the Exchange Act report.

The Commission recognizes that a Covered Entity preparing multiple UK compliance reports each year may find it difficult to submit to the Commission multiple UK compliance reports throughout the year, each with a chief compliance officer or senior officer certification and a section addressing the Covered Entity's compliance with U.S. requirements. However, on balance the Commission believes that these elements are necessary to achieve a regulatory outcome comparable to the Exchange Act, and is retaining the requirement for all reports to include them. The commenter's suggested alternative—to allow a Covered Entity to create a single annual report regarding its SBS business—amounts to a request to allow a Covered Entity to prepare a bespoke compliance report outside of the requirements of both the Exchange Act and the UK regulatory framework. The Commission believes this bespoke

that a Covered Entity's certification would include statements that the certification is ''to the best of the certifier's knowledge and reasonable belief'' and that the report is accurate and complete ''in all material respects'').

[357] Exchange Act rule 15Fk–1(c)(2)(ii)(D); *see also* Exchange Act rule 15Fk–1(e)(2) (defining ''senior officer'' as ''the chief executive officer or other equivalent officer'').

[358] *See* para. (d)(2)(ii)(B) of the Order.

[359] *See* para. (d)(4) of the Order. In practice, a Covered Entity may satisfy this condition by identifying relevant Order conditions and reporting on the implementation and effectiveness of its controls with regard to compliance with applicable Exchange Act requirements and relevant provisions of the Order.

[360] *See* SIFMA 5/3/2021 Letter at 21 and Appendix A part (d)(2). With regard to the French Substituted Compliance Notice and Proposed Order, SIFMA supported an additional timing standard that would provide for an annual submission 15 days after the submission to the French regulatory authority. The Commission addresses SIFMA's comment in connection with its consideration of French authorities' application for substituted compliance.

[361] *See* para. (d)(2)(ii)(D) of the Order.

[362] In its comment on the same provision in the French Substituted Compliance Notice and Proposed Order, the commenter asked the Commission to permit a Covered Entity to make an annual submission of the foreign compliance report within 15 days after submission of that report to the foreign regulatory authority. The commenter explained that, absent clarification, the Order would appear to require a Covered Entity to provide the Commission its foreign compliance report within 30 days following the deadline for the Covered Entity to file its annual financial report with the Commission, without regard to when the Covered Entity prepares its foreign compliance report. *See* SIFMA 5/3/2021 Letter at 19–20 and Appendix A part (d)(2), available at: *https://www.sec.gov/comments/s7-22-20/s72220.htm.*

[363] *See* para. (d)(2)(ii)(E) of the Order.

report would be inconsistent with its mandate to make a positive substituted compliance determination only when the Covered Entity complies with comparable foreign requirements, and is not amending the Order to provide this option. A Covered Entity that produces multiple UK compliance reports each year, but wishes to prepare a single annual compliance report addressing its compliance with Exchange Act requirements, is not required to use substituted compliance for chief compliance officer requirements, even if it chooses to use substituted compliance for other Exchange Act requirements. Such a Covered Entity instead could choose to comply directly with Exchange Act chief compliance officer requirements, including requirements related to the annual compliance report, rather than use substituted compliance for those requirements.

Third, the commenter requested that the proposed Order be modified to narrow the scope of the compliance reports provided to the Commission, stating that the Covered Entity should be permitted to provide the Commission its UK compliance reports only ''to the extent that they are related to a Covered Entity's business as an [SBS Entity].'' [364] The commenter stated that it would be ''disproportionate and unnecessary'' to require the Covered Entity to provide the Commission all of its UK compliance reports prepared pursuant to UK MiFID Org Reg article 22(2)(c).[365] The Commission disagrees, and believes that the Commission should be fully informed—consistent with the scope of UK MiFID Org Reg article 22(2)(c)—as to the ''implementation and effectiveness'' of the Covered Entity's ''overall control environment for investment services and activities,'' as well as associated risks, complaints handling and remedies. The alternative approach of apportioning compliance reports into two buckets, and providing the Commission reports in only one of the buckets, does not match the analytic approach of considering the Exchange Act and UK frameworks as a whole. Accordingly, the Commission is retaining the requirement that a Covered Entity provide all reports required pursuant to UK MiFID Org Reg article 22(2)(c) to the Commission.

3. Antitrust Requirements

The Commission did not receive any comments on the absence of a positive substituted compliance determination for antitrust requirements in Exchange Act section 15F(j)(6) (and related internal supervision requirements of Exchange Act rule 15Fh–3(h)(2)(iii)(I)) in the proposed Order. The Commission continues to believe that allowing an alternative means of compliance would not lead to outcomes comparable to the Exchange Act, and is not making a positive substituted compliance determination for those requirements.[366]

VII. Substituted Compliance for Counterparty Protection Requirements

A. Proposed Approach

The FCA Application in part requested substituted compliance in connection with counterparty protection requirements relating to:

- Disclosure of material risks and characteristics and material incentives or conflicts of interest—Requirements that an SBS Entity disclose to certain security-based swap counterparties certain information about the material risks and characteristics of the security-based swap, as well as material incentives or conflicts of interest that the SBS Entity may have in connection with the security-based swap.
- ''Know your counterparty''—Requirements that an SBS Entity establish, maintain, and enforce written policies and procedures to obtain and retain certain information regarding a security-based swap counterparty that is necessary for conducting business with that counterparty.
- Suitability—Requirements for a security-based swap dealer to undertake reasonable diligence to understand the potential risks and rewards of any recommendation of a security-based swap or trading strategy involving a security-based swap that it makes to certain counterparties and to have a reasonable basis to believe that the recommendation is suitable for the counterparty.
- Fair and balanced communications—Requirements that an SBS Entity communicate with security-based swap counterparties in a fair and balanced manner based on principles of fair dealing and good faith.
- Daily mark disclosure—Requirements that an SBS Entity provide daily mark information to certain security-based swap counterparties.
- Clearing rights disclosure—Requirements that an SBS Entity provide certain counterparties with information regarding clearing rights under the Exchange Act.

Taken as a whole, these counterparty protection requirements help to ''bring professional standards of conduct to, and increase transparency in, the security-based swap market and to require registered [entities] to treat parties to these transactions fairly.'' [367]

The proposed Order provided for substituted compliance in connection with disclosure of material risks and characteristics, disclosure of material incentives or conflicts of interest, ''know your counterparty,'' suitability, fair and balanced communications, and daily mark disclosure requirements.[368] In proposing to provide conditional substituted compliance for these requirements, the Commission preliminarily concluded that the relevant UK requirements in general would produce regulatory outcomes that are comparable to requirements under the Exchange Act, by subjecting Covered Entities to obligations that promote standards of professional conduct, transparency, and the fair treatment of parties.

As proposed, substituted compliance for these requirements would be subject to certain conditions to help ensure the comparability of outcomes. First, under the proposed Order, substituted compliance for disclosure of material risks and characteristics, disclosure of material incentives or conflicts of interest, ''know your counterparty,'' suitability, and fair and balanced communications requirements would be conditioned on Covered Entities being subject to, and complying with, relevant UK requirements.[369] Second, the

[364] *See* SIFMA 5/3/2021 Letter at 21 and Appendix A part (d)(2).

[365] *See* SIFMA 5/3/2021 Letter at 21.

[366] Non-U.S. SBS Entities should assess the applicability of the Exchange Act's antitrust prohibitions to their security-based swap businesses.

[367] *See* Business Conduct Adopting Release, 81 FR at 30065. These transaction-level requirements apply only to a non-U.S. SBS Entity's transactions with U.S. counterparties (apart from certain transactions conducted through a foreign branch of the U.S. counterparty), or to transactions arranged, negotiated, or executed in the United States. *See* Exchange Act rule 3a71–3(c) (exception from business conduct requirements for a security-based swap dealer's ''foreign business''); *see also* Exchange Act rule 3a71–3(a)(3), (8), and (9) (definitions of ''transaction conducted through a foreign branch,'' ''U.S. business'' and ''foreign business'').

[368] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18414–15.

[369] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18392 n.134. Each of the comparable UK requirements listed in the proposed Order applies to a uniquely defined set of UK-authorized firms. *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18392 n.137. To assist UK firms in determining whether they are subject to these requirements, the Commission preliminarily determined that any Covered Entity would be subject to the required UK requirements related to disclosure of material risks and characteristics, disclosure of material incentives or conflicts of interest, suitability, and fair and balanced communications and thus eligible to apply substituted compliance in these areas. The Commission also preliminarily determined that any

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proposed Order would additionally condition substituted compliance for suitability requirements on the counterparty being a per se ''professional client'' as defined in FCA COBS (rather an elective professional client or a retail client [370]) and not a ''special entity'' as defined in Exchange Act section 15F(h)(2)(C) and Exchange Act rule 15Fh–2(d).[371] Finally, in the proposed Order the Commission preliminarily viewed UK daily portfolio reconciliation requirements as comparable to Exchange Act daily mark disclosure requirements.[372] These daily portfolio reconciliation requirements apply to portfolios of a financial counterparty or a non-financial counterparty subject to the clearing obligation in UK EMIR in which the counterparties have 500 or more OTC derivatives contracts outstanding with each other.[373] The Commission preliminarily viewed UK portfolio reconciliation requirements for other types of portfolios, which may be reconciled less frequently than each business day, as not comparable to Exchange Act daily mark requirements.[374] Accordingly, the proposed Order would condition substituted compliance for daily mark requirements on the Covered Entity being required to reconcile, and in fact reconciling, the portfolio containing the relevant security-based swap on each business day pursuant to relevant UK requirements.[375]

The proposed Order would not provide substituted compliance in connection with Exchange Act requirements for SBS Entities to disclose a counterparty's clearing rights under Exchange Act section 3C(g)(5).[376] The FCA Application argued that certain UK provisions related to a counterparty's clearing rights in the UK are comparable to requirements to disclose the counterparty's Exchange Act-based clearing rights. Because these UK provisions do not require disclosure of these clearing rights, the Commission preliminarily viewed the UK clearing provisions as not comparable to Exchange Act clearing rights disclosure requirements.

B. Commenter Views and Final Provisions

Having considered commenters' recommendations regarding the counterparty protection requirements, the Commission is making positive substituted compliance determinations in connection with disclosure of material risks and characteristics, disclosure of material incentives or conflicts of interest, ''know your counterparty,'' suitability, fair and balanced communications, and daily mark disclosure requirements. With respect to Exchange Act clearing rights disclosure requirements, however, consistent with the proposed Order the Commission is not providing substituted compliance. The Order is largely consistent with the proposed Order except for removing one UK requirement listed in two sections of the Order and correcting a typographical error.[377]

One commenter expressed general support for the proposed approach toward substituted compliance for the counterparty protection provisions.[378] Another commenter stated that UK requirements are not sufficiently comparable to Exchange Act requirements.[379] The Commission continues to believe that, taken as a whole, applicable requirements under UK law subject Covered Entities to obligations that promote standards of professional conduct, transparency, and the fair treatment of parties, and thus produce regulatory outcomes that are comparable to the outcomes associated with the relevant counterparty protection requirements under the Exchange Act. The Commission recognizes that there are differences between the approaches taken by disclosure of material risks and characteristics, disclosure of material incentives or conflicts of interest, ''know your counterparty,'' suitability, fair and balanced communications, and daily mark disclosure requirements under the Exchange Act, on the one hand, and relevant UK requirements, on the other hand. The Commission continues to view those differences as not so material as to be inconsistent with substituted compliance within the requisite outcomes-oriented context.

To help ensure the comparability of outcomes, substituted compliance for counterparty protection requirements is subject to certain conditions. Substituted compliance for disclosure of material risks and characteristics, disclosure of material incentives or conflicts of interest, ''know your counterparty,'' suitability, and fair and balanced communications requirements is conditioned on the Covered Entity being subject to, and complying with, relevant UK requirements.[380] Substituted compliance for daily mark disclosure requirements is conditioned on the Covered Entity being required to reconcile, and in fact reconciling, the portfolio containing the relevant security-based swap on each business day pursuant to relevant UK requirements.[381] Substituted compliance for suitability requirements additionally is conditioned on the counterparty being a per se ''professional client'' mentioned in FCA COBS 3.5.2R (*i.e.,* not an elective professional client or a retail client) and not a ''special entity'' as defined in Exchange Act section 15F(h)(2)(C) and Exchange Act rule 15Fh–2(d).[382] A Covered Entity that is unable to comply with a condition—and thus is not eligible to use substituted compliance for the particular set of Exchange Act counterparty protection requirements related to that condition—nevertheless

Covered Entity that is an ''IFPRU investment firm,'' ''UK bank'' or ''UK designated investment firm,'' each as defined for purposes of UK law, would be subject to all of the required UK requirements related to ''know your counterparty'' requirements and thus eligible to apply substituted compliance for ''know your counterparty'' requirements. Finally, the Commission preliminarily determined that any Covered Entity that is a ''financial counterparty'' would be subject to all of the required UK requirements related to daily mark disclosure and thus eligible to apply substituted compliance for daily mark disclosure requirements. *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18392–93.

[370] FCA COBS 3.5 describes which clients are ''professional clients.'' FCA COBS 3.5.2R describes the types of clients considered to be professional clients unless the client elects non-professional treatment; these clients are per se professional clients. FCA COBS 3.5.3R describes the types of clients who may be treated as professional clients on request; these clients are elective professional clients. *See* FCA COBS 3.5. Retail clients are those that are not professional clients (nor eligible counterparties, in contexts other than suitability assessments in which treatment as an eligible counterparty is permitted). *See* FCA COBS 3.4.1R.

[371] 15 U.S.C. 78*o*–10(h)(2)(C); 17 CFR 240.15Fh–2(d). *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18393–94.

[372] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18393.

[373] *See* UK EMIR RTS article 13(3)(a)(i); UK EMIR article 10.

[374] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18393.

[375] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18393.

[376] 15 U.S.C. 78c–3(g)(5).

[377] *See* paras. (e)(1)(i), (e)(5)(ii) and (e)(4)(i)(A) of the Order.

[378] *See* SIFMA 5/3/2021 Letter at 21. The commenter also requested that the Commission not require a Covered Entity to be subject to and comply with some of the UK counterparty protection requirements listed in the proposed Order. *See* SIFMA 5/3/2021 Letter at 21 and Appendix A part (e). The Commission addresses those requests in the relevant sections of this part VII below.

[379] *See* Better Markets Letter at 2. The commenter also stated that, if the Commission nevertheless makes a positive substituted compliance determination, it must at a minimum ensure that the conditions in the proposed Order ''are applied with full force and without exceptions or dilution.'' The Commission addresses that comment in the relevant sections of this part VII below.

[380] *See* paras. (e)(1) through (5) of the Order.

[381] *See* para. (e)(6) of the Order.

[382] *See* para. (e)(4)(ii) of the Order.

may use substituted compliance for another set of Exchange Act requirements addressed in the Order if it complies with the conditions to the relevant parts of the Order.

Under the Order, substituted compliance for counterparty protection requirements (relating to disclosure of information regarding material risks and characteristics, disclosure of information regarding material incentives or conflicts of interest, ''know your counterparty,'' suitability, fair and balanced communications, and daily mark disclosure) is not subject to a condition that the Covered Entity apply substituted compliance for related recordkeeping requirements in Exchange Act rules 18a–5 and 18a–6. A Covered Entity that applies substituted compliance for one or more counterparty protection requirements, but does not apply substituted compliance for the related recordkeeping requirements in Exchange Act rules 18a–5 and 18a–6, will remain subject to the relevant provisions of Exchange Act rules 18a–5 and 18a–6. Those rules require the Covered Entity to make and preserve records of its compliance with Exchange Act counterparty protection requirements and of its security-based swap activities required or governed by those requirements. A Covered Entity that applies substituted compliance for a counterparty protection requirement, but complies directly with related recordkeeping requirements in rules 18a–5 and 18a–6, therefore must make and preserve records of its compliance with the relevant conditions to the Order and of its security-based swap activities required or governed by those conditions and/or referenced in the relevant parts of rules 18a–5 and 18a–6.

The Commission details below its consideration of comments on the proposed Order.

1. Disclosure of Information Regarding Material Risks and Characteristics

A commenter requested that the Commission not require a Covered Entity to be subject to and comply with some of these specified requirements.[383] By contrast, another commenter stated that, if the Commission makes a positive substituted compliance determination, it must at a minimum ensure that the conditions in the proposed Order ''are applied with full force and without exceptions or dilution.'' [384] The Commission details below its consideration of each of these requests.

First, the commenter stated that FCA COBS 2.2A.2R(1)(d), 6.1ZA.11R, 6.1ZA.12R, and 6.1ZA.14UK and UK MiFID Org Reg article 50 relate to disclosure of costs and charges and thus go beyond the scope of Exchange Act material risks and characteristics disclosure requirements. Exchange Act rule 15Fh–3(b)(1) requires a Covered Entity, before entering into a security-based swap, to disclose to certain counterparties material information about the security-based swap in a manner reasonably designed to allow the counterparty to assess the material risks and characteristics of the security-based swap, which may include the material economic terms of the security-based swap and the rights and obligations of the parties during the term of the security-based swap. The material economic terms of a security-based swap and the rights and obligations of the parties include the costs and charges associated with the security-based swap. Accordingly, the Commission is retaining the references to these provisions.

Second, the commenter stated that FCA COBS 2.2A.2R(1)(c) relates to insurance-based investments and thus goes beyond the scope of Exchange Act material risks and characteristics disclosure requirements. FCA COBS 2.2A.2R(1)(c) would require a Covered Entity to provide its client in good time appropriate information about the distribution of ''insurance-based investment products.'' The Commission is not making a determination whether an ''insurance-based investment product,'' as defined for purposes of this provision, could also be a security-based swap. However, even without this provision, FCA COBS 2.2A.2R(b) would require the Covered Entity to provide its client in good time appropriate information about any relevant ''financial instruments,'' which are a defined set of instruments to which this and other MiFID-based provisions apply. The general condition in paragraph (a)(3) of the Order would require any Covered Entity using substituted compliance for Exchange Act material risks and characteristics disclosure requirements to ensure that its relevant security-based swap activities (in this case, disclosure to counterparties before entering into a security-based swap) constitute ''MiFID or equivalent third country business,'' which is defined to include the same set of instruments in the definition of ''financial instruments.'' As a result, the disclosures of a Covered Entity applying substituted compliance for Exchange Act material risks and characteristics disclosure requirements would always be in relation to a security-based swap that is a ''financial instrument.'' Accordingly, the Commission believes it is appropriate to delete the reference to FCA COBS 2.2A.2R(1)(c) in the Order.

Third, the commenter stated that FCA COBS 6.1ZA.9UK and UK MiFID Org Reg article 49 relate to information about the safeguarding of client assets and thus go beyond the scope of Exchange Act material risks and characteristics disclosure requirements. These provisions would require a Covered Entity to inform its client about the risks of the Covered Entity placing client assets, which would include the relevant security-based swap and funds related to it, to be held by a third party, the risks of the Covered Entity holding client assets in an omnibus account, the risks of holding client assets that are not segregated from the assets of the Covered Entity or a third party holding the client's assets and the risks of the Covered Entity entering into securities financing transactions using client assets. A Covered Entity also would have to inform the client when the relevant security-based swap is held in an account subject to the laws of a non-UK jurisdiction and indicate that client rights relating to the security-based swap may differ from those under UK law. A Covered Entity also would have to inform the client about any security interest, lien, or right of set-off that the Covered Entity or a depository may have over client assets. In comparison, Exchange Act rule 15Fh–3(b)(1) requires a Covered Entity, before entering into a security-based swap, to disclose to certain counterparties material information about the security-based swap in a manner reasonably designed to allow the counterparty to assess the material risks and characteristics of the security-based swap, which may include market, credit, liquidity, foreign currency, legal, operational, and any other applicable risks of the security-based swap. Legal and operational risks of a security-based swap include the types of risks to client assets that FCA COBS 6.1ZA.9UK and UK MiFID Org Reg article 49 would require the Covered Entity to disclose. Accordingly, the Commission is retaining the references to these provisions.

Finally, the commenter stated that FCA COBS 6.2B.33R and 9A.3.6R relate to disclosure about whether a firm is providing independent advice or will undertake a periodic suitability assessment and thus go beyond the scope of Exchange Act material risks and characteristics disclosure

[383] *See* SIFMA 5/3/2021 Letter at 21 and Appendix A part (e)(1).

[384] *See* Better Markets Letter at 2.

requirements.[385] As described above, Exchange Act rule 15Fh–3(b)(1) requires a Covered Entity, before entering into a security-based swap, to disclose to certain counterparties material information about the security-based swap in a manner reasonably designed to allow the counterparty to assess the material risks and characteristics of the security-based swap, which may include the material economic terms of the security-based swap and the rights and obligations of the parties during the term of the security-based swap. The Commission believes that a counterparty would consider the independence of the Covered Entity's advice and the presence or absence of a periodic suitability assessment in the counterparty's assessment of these risks and characteristics. The holistic approach taken by the Commission in considering whether regulatory requirements are comparable further warrants the inclusion of these provisions in the Order. Accordingly, the Commission is retaining the references to these provisions.

2. Disclosure of Information Regarding Material Incentives or Conflicts of Interest

A commenter requested that the Commission not require a Covered Entity to be subject to and comply with FCA COBS 2.3A.5R, 2.3A.6R, 2.3A.7E, or 2.3A.11R through 2.3A.14R, stating that these provisions relate to third-party payments and thus go beyond the scope of Exchange Act material incentives or conflicts of interest disclosure requirements.[386] By contrast, another commenter stated that, if the Commission makes a positive substituted compliance determination, it must at a minimum ensure that the conditions in the proposed Order ''are applied with full force and without exceptions or dilution.'' [387] These provisions would require a Covered Entity to refrain from paying to, or accepting from, third parties certain fees, commissions or non-monetary benefits in connection with providing an investment service (inducements) and, in circumstances in which the general prohibition on inducements does not apply, to disclose to the client the existence, nature, and amount of the inducement prior to providing the service and in a manner that is comprehensive, accurate, and understandable. In comparison, Exchange Act rule 15Fh–3(b)(2) requires a Covered Entity, before entering into a security-based swap, to disclose to certain counterparties material information about the security-based swap in a manner reasonably designed to allow the counterparty to assess the material incentives or conflicts of interest that the Covered Entity may have in connection with the security-based swap, including any compensation or other incentives from any source other than the counterparty. Disclosure of this compensation or other incentives would include disclosure of the existence, nature, and amount of an inducement that FCA COBS 2.3A.5R, 2.3A.6R, 2.3A.7E, and 2.3A.11R through 2.3A.14R would require the Covered Entity to disclose. Accordingly, the Commission is retaining the references to these provisions.

3. ''Know Your Counterparty''

A commenter requested that the Commission not require a Covered Entity to be subject to and comply with some of these specified requirements.[388] By contrast, another commenter stated that, if the Commission makes a positive substituted compliance determination, it must at a minimum ensure that the conditions in the proposed Order ''are applied with full force and without exceptions or dilution.'' [389] The Commission details below its consideration of each of these requests.

First, the commenter stated that UK MiFID Org Reg articles 21, 22, 25, and 26 and applicable parts of Annex I relate to organizational requirements, compliance, responsibility of senior management, complaints handling, and associated recordkeeping and thus go beyond the scope of Exchange Act ''know your counterparty'' requirements. In addition to these provisions cited by the commenter, the proposed Order would require (with no objection from the commenter) a Covered Entity using substituted compliance for Exchange Act ''know your counterparty'' requirements to be subject to and comply with FCA SYSC 6.1.1R, which implements MiFID article 16(2) in the UK and would require a Covered Entity to establish, implement, and maintain adequate policies and procedures sufficient to ensure the Covered Entity's compliance with its obligations under UK financial services laws. This requirement relates to the requirement in Exchange Act rules 15Fh–3(e)(1) and (2) for the Covered Entity to establish, maintain, and enforce written policies and procedures to obtain and retain a record of the essential facts about the counterparty that are necessary for complying with applicable laws, regulations, and rules and for implementing the Covered Entity's credit and operational risk management policies. UK MiFID Org Reg articles 21, 22, 25, and 26 and applicable parts of Annex I are regulations that implement MiFID article 16(2). They provide additional detail about the Covered Entity's required policies and procedures under the UK framework, and as such are relevant to the policies and procedures required under Exchange Act rule 15Fh–3(e). Accordingly, the Commission is retaining the references to these provisions.

Second, the commenter stated that FCA SYSC 4.1.1R(1) relates to general organizational requirements and thus goes beyond the scope of Exchange Act ''know your counterparty'' requirements. FCA SYSC 4.1.1R(1) would require the Covered Entity to have robust governance arrangements, including effective processes to identify, manage, monitor, and report the risks it is or might be exposed to. This requirement relates to the requirement in Exchange Act rule 15Fh–3(e)(2) for the Covered Entity to establish, maintain, and enforce written policies and procedures to obtain and retain a record of the essential facts about the counterparty that are necessary for implementing the Covered Entity's credit and operational risk management policies. Accordingly, the Commission is retaining the reference to this provision.

Third, the commenter recommended deleting FCA IFPRU 2.2.7R(2) and 2.2.32R because they do not apply to banks or PRA-designated investment firms and the commenter expects only banks and PRA-designated investment firms to apply substituted compliance pursuant to the Order. These FCA IFPRU provisions apply to smaller investment firms not regulated by the PRA and are nearly identical to provisions that apply to banks and PRA-designated investment firms. The proposed Order would not require a Covered Entity that is a bank or PRA-designated investment firm to be subject to and comply with these provisions. Rather, the proposed Order would require each Covered Entity to be subject to and comply with either these IFPRU provisions (if it is a smaller investment firm) or analogous PRA requirements (if it is a bank or PRA-designated investment firm). Moreover, the FCA Application requested substituted compliance for all MiFID

[385] *See* SIFMA 5/3/2021 Letter Appendix A part (e)(1).

[386] *See* SIFMA 5/3/2021 Letter at 21 and Appendix A part (e)(1).

[387] *See* Better Markets Letter at 2.

[388] *See* SIFMA 5/3/2021 Letter at 21 and Appendix A part (e)(3).

[389] *See* Better Markets Letter at 2.

investment firms and third country investment firms, and was not limited to banks and PRA-designated investment firms. Accordingly, the Commission is retaining the references to these provisions.

Fourth, the commenter stated that PRA General Organisational Requirement 2.1 relates to high-level governance requirements and thus goes beyond the scope of Exchange Act ''know your counterparty'' requirements. The provision is identical in all material respects to FCA SYSC 4.1.1R(1) and serves as the PRA's version of that requirement for PRA-regulated Covered Entities. Accordingly, the Commission is retaining the reference to this provision.

Finally, the commenter stated that PRA Internal Capital Adequacy Assessment Rule 10.1 relates to assessment of the capital needed to cover risks and thus goes beyond the scope of Exchange Act ''know your counterparty'' requirements. This provision would require a Covered Entity to implement policies and processes to evaluate and manage the exposure to operational risk. These policies and processes are related to the requirement in Exchange Act rule 15Fh–3(e)(2) for the Covered Entity to establish, maintain, and enforce written policies and procedures to obtain and retain a record of the essential facts about the counterparty that are necessary for implementing the Covered Entity's credit and operational risk management policies. Accordingly, the Commission is retaining the reference to this provision.

4. Suitability

A commenter requested that the Commission amend these conditions.[390] By contrast, another commenter stated that, if the Commission makes a positive substituted compliance determination, it must at a minimum ensure that the conditions in the proposed Order ''are applied with full force and without exceptions or dilution.'' [391] The Commission details below its consideration of each of these requests.

First, the commenter requested that the Commission not require a Covered Entity to be subject to and comply with some of the UK suitability requirements specified in the proposed Order.[392] The commenter stated that FCA COBS 4.2.1R is more appropriately addressed in the section of the order relating to fair and balanced communications and that MiFID Org Reg article 21(1)(b) is more appropriately addressed in the section of the order relating to internal supervision. The commenter further stated that FCA SYSC 5.1.5AAR and 5.1.5ABR and UK MiFID Org Reg article 21(1)(d) go beyond the scope of Exchange Act suitability requirements.

Exchange Act rule 15Fh–3(f) requires an SBS Entity, when making certain security-based swap recommendations to a counterparty, to undertake reasonable diligence to understand the potential risks and rewards associated with the recommendation (the reasonable basis suitability standard) and to have a reasonable basis to believe that the recommendation is suitable for the counterparty (the counterparty-specific suitability standard).[393] FCA SYSC 5.1.5AAR and 5.1.5ABR, which implement MiFID article 25(1), would require a Covered Entity to ensure that individuals making personal recommendations to clients in relation to a relevant security-based swap have the necessary knowledge and competence so as to ensure that the Covered Entity is able to meet its obligations under FCA rules that implement MIFID articles 24 and 25 and the related provisions of the UK MiFID Org Reg. FCA COBS 9A.2.1R and 9A.2.16R, which implement MiFID article 25(2), would require the Covered Entity to obtain information about a client necessary to ensure that it makes only recommendations that are suitable for the client, and thus are relevant to the Exchange Act counterparty-specific suitability standard. FCA SYSC 5.1.5AAR and 5.1.5ABR thus would require the Covered Entity to ensure that recommendations to clients are made with the knowledge and competence necessary to fulfill the Covered Entity's obligation under FCA COBS 9A.2.1R and 9A.2.16R to make only suitable recommendations. This knowledge and competence requirement in FCA SYSC 5.1.5AAR and 5.1.5ABR is directly related to the Exchange Act reasonable basis suitability standard.

Moreover, FCA COBS 4.2.1R, which implements MiFID article 24(3), is particularly relevant to the Exchange Act reasonable basis standard. FCA COBS 4.2.1R, together with FCA SYSC 5.1.5AAR and 5.1.5ABR, would require the Covered Entity to ensure that individuals making recommendations have the knowledge and competence to communicate about the relevant security-based swap in a way that is fair, clear, and not misleading. The Commission believes that in order to meet the FCA requirement to communicate in a fair, clear, and not misleading manner, the Covered Entity's due diligence would reflect that individuals engaged in such communication understand the potential risks and rewards of the recommendation in a manner that is comparable to the requirement in Exchange Act rule 15Fh–3(f)(1)(i). MiFID Org Reg articles 21(1)(b) and (d), in turn, would require the Covered Entity to ensure that its personnel have the skills, knowledge, and expertise, and be aware of the procedures, necessary to properly discharge their responsibilities, which include their suitability obligations. These requirements again relate to the Exchange Act reasonable basis standard because they would require the Covered Entity to ensure that personnel making recommendations are equipped with the requisite training and information to be able to communicate about the relevant security-based swap in a way that complies with its communication and suitability obligations in FCA COBS and FCA SYSC.

For these reasons, the Commission is retaining in the Order the references to these UK requirements that the commenter asked to delete, and thus is requiring a Covered Entity to be subject to and comply with these UK requirements if the Covered Entity wishes to make use of substituted compliance for Exchange Act suitability requirements. Separately, as stated by the commenter, the proposed Order erroneously referred to FCA COBS 9A.1.16R instead of FCA COBS 9A.2.16R, and the Commission is amending the Order to correct this error.[394]

Second, the commenter requested that the Commission change the condition to substituted compliance for Exchange Act suitability requirements that would require the Covered Entity's counterparty to be a ''professional client'' mentioned in FCA COBS 3.5.2R. Professional clients mentioned in FCA COBS 3.5.2R are per se professional clients, a category of clients that generally includes those with more experience, knowledge, expertise, and resources and that excludes elective professional clients and retail clients. The commenter requested that the Commission replace FCA COBS 3.5.2R with FCA COBS 3.5.1R, a provision that refers to both per se and elective professional clients. Elective professional clients generally have less experience, knowledge, expertise, and/or resources than per se professional

[390] *See* SIFMA 5/3/2021 Letter at 21 and Appendix A part (e)(4).

[391] *See* Better Markets Letter at 2.

[392] *See* SIFMA 5/3/2021 Letter at 21 and Appendix A part (e)(4).

[393] *See* Exchange Act rule 15Fh–3(f)(1).

[394] *See* para. (e)(4)(i)(A) of the Order.

clients.[395] Because UK suitability requirements permit a Covered Entity, when conducting a suitability analysis for elective professional clients, to make certain assumptions,[396] while the Exchange Act permits a similar mechanism only for institutional counterparties, the Commission believes that UK suitability requirements are comparable only in respect of per se professional clients. Accordingly, the Commission is retaining the condition requiring the Covered Entity's counterparty to be a per se professional client and is not expanding that condition to permit Covered Entities to apply substituted compliance for Exchange Act suitability requirements when its counterparty is an elective professional client.

5. Fair and Balanced Communications

A commenter requested that the Commission not require a Covered Entity to be subject to and comply with some of these specified requirements.[397] By contrast, another commenter stated that, if the Commission makes a positive substituted compliance determination, it must at a minimum ensure that the conditions in the proposed Order ''are applied with full force and without exceptions or dilution.'' [398] The Commission details below its consideration of each of these requests.

First, the commenter asked the Commission not to require a Covered Entity to be subject to and comply with FCA COBS 2.2A.2R(1)(d), 6.1ZA.11R, 6.1ZA.12R, and 6.1ZA.13R because they relate to disclosure of costs and charges and thus go beyond the scope of Exchange Act fair and balanced communications requirements.[399] Exchange Act rule 15Fh–3(g)(1) requires a Covered Entity's communications to provide a sound basis for evaluating the facts with regard to any particular security-based swap or trading strategy involving a security-based swap. The Commission believes that information about costs and charges required to be disclosed under these UK requirements is comparable to one type of information that would help to provide a sound basis for evaluating the facts as required under 15Fh–3(g)(1). Accordingly, the Commission is retaining the references to these provisions.

Second, the commenter asked the Commission not to require a Covered Entity to be subject to and comply with FCA COBS 2.2A.2R(1)(c) because it relates to insurance-based investments and thus goes beyond the scope of Exchange Act fair and balanced communications requirements.[400] FCA COBS 2.2A.2R(1)(c) would require a Covered Entity to provide its client in good time appropriate information about the distribution of ''insurance-based investment products.'' The Commission is not making a determination whether an ''insurance-based investment product,'' as defined for purposes of this UK provision, could also be a security-based swap. However, even without this provision, FCA COBS 2.2A.2R(1)(b) would require the Covered Entity to provide its client in good time appropriate information about any relevant ''financial instruments,'' which are a defined set of instruments to which this and other MiFID-based provisions apply. The general condition in paragraph (a)(3) of the Order would require any Covered Entity using substituted compliance for Exchange Act fair and balanced communications requirements to ensure that its relevant security-based swap activities (in this case, communications with counterparties) constitute ''MiFID or equivalent third country business,'' which is defined to include the same set of instruments in the definition of ''financial instruments.'' As a result, the communications of a Covered Entity applying substituted compliance for Exchange Act fair and balanced communications requirements would always be in relation to a security-based swap that is a ''financial instrument.'' Accordingly, the Commission believes it is appropriate to delete the reference to FCA COBS 2.2A.2R(1)(c) in the Order.

Third, the commenter asked the Commission not to require a Covered Entity to be subject to and comply with FCA COBS 2.2A.3R because it relates to the format of disclosure and thus goes beyond the scope of Exchange Act fair and balanced communications requirements.[401] Exchange Act rule 15Fh–3(g)(1) requires a Covered Entity's communications to provide a sound basis for evaluating the facts with regard to any particular security-based swap or trading strategy involving a security-based swap. FCA COBS 2.2A.3R would require the Covered Entity to provide the information required by FCA COBS 2.2A.2R in a comprehensive form in such a manner that the client is reasonably able to understand the nature and risks of the investment service and of the specific type of financial instrument that is being offered and, consequently, to take investment decisions on an informed basis. This requirement to provide information in a manner that the client is reasonably able to take informed investment decisions is well within the scope of the Exchange Act requirement to provide counterparties a sound basis for evaluating the relevant facts of a transaction or strategy. Accordingly, the Commission is retaining the reference to this provision.

Fourth, the commenter asked the Commission not to require a Covered Entity to be subject to and comply with FCA COBS 6.1ZA.8UK because it relates to portfolio management services and thus goes beyond the scope of Exchange Act fair and balanced communications requirements. FCA COBS 6.1ZA.8UK would require a Covered Entity, when providing or proposing to provide portfolio management services, to provide certain information to its client to enable the client to assess the Covered Entity's performance. The Commission is not making a determination whether particular examples of ''portfolio management,'' as the term is used in this provision, also constitute dealing in a security-based swap for purposes of the Exchange Act. However, to the extent that FCA COBS 6.1ZA.8UK applies to a Covered Entity's communication, it is an element of the UK's fair and balanced communications framework that compares to Exchange Act requirements to provide a sound basis for evaluating the facts with regard to a security-based swap or trading strategy involving a security-based swap. If the Covered Entity is applying substituted compliance in relation to such a communication, the Commission believes that it is appropriate to require the Covered Entity to comply with this requirement. Accordingly, the Commission is retaining the reference to this provision.

Fifth, the commenter asked the Commission not to require a Covered Entity to be subject to and comply with UK MAR Investment Recommendations Regulation articles 3 and 4 and UK MAR articles 12(1)(c), 15, and 20(1) because they relate to investment recommendations and market manipulation and thus go beyond the scope of Exchange Act fair and balanced communications requirements. Exchange Act rule 15Fh–3(g) requires in relevant part that an SBS Entity's communications with counterparties provide a sound basis for evaluating the facts with regard to a particular security-based swap or trading strategy involving a security-based swap; not imply that

[395] *See, e.g.,* FCA COBS 3.5.3R.

[396] *See, e.g.,* UK MiFID Org Reg article 54(3).

[397] *See* SIFMA 5/3/2021 Letter at 21 and Appendix A part (e)(5).

[398] *See* Better Markets Letter at 2.

[399] *See* SIFMA 5/3/2021 Letter at 21 and Appendix A part (e)(5).

[400] *See* SIFMA 5/3/2021 Letter at 21 and Appendix A part (e)(5).

[401] *See* SIFMA 5/3/2021 Letter at 21 and Appendix A part (e)(5).

past performance will recur; not make exaggerated or unwarranted claims, opinions, or forecasts; and balance statements about potential opportunities or advantages of a security-based swap with an equally detailed statement of the corresponding risks. UK MAR article 20(1) would require the Covered Entity to present recommendations in a manner that ensures the information is objectively presented and to disclose interests and conflicts of interest concerning the financial instruments to which the information relates. UK MAR Investment Recommendations Regulation article 3 would require a Covered Entity to communicate only recommendations that present facts in a way that they are clearly distinguished from interpretations, estimates, opinions, and other types of non-factual information; label clearly and prominently projections, forecasts, and price targets; indicate the relevant material assumptions and substantially material sources of information; and include only reliable information or a clear indication when there is doubt about reliability. UK MAR Investment Recommendations Regulation article 4 would require the Covered Entity to provide in its recommendation additional information about the factual basis of its recommendation. UK MAR articles 12(1)(c) and 15 would require the Covered Entity to refrain from disseminating information that gives or is likely to give false or misleading signals as to the supply of, demand for, or price of, a financial instrument or secures or is likely to secure the price of one or several financial instruments at an abnormal or artificial level, if the Covered Entity knows or ought to know that the information is false or misleading. These requirements form part of the UK's framework for fair and balanced communications, and the Commission believes that together they relate to Exchange Act rule 15Fh–3(g)'s requirements regarding presentation of factual information described above. Accordingly, the Commission is retaining the references to these provisions.

6. Daily Mark Disclosure

A commenter requested that the Commission not require a Covered Entity to be subject to and comply with UK EMIR article 11(2), stating that it is not related to portfolio reconciliation.[402] By contrast, another commenter stated that, if the Commission makes a positive substituted compliance determination, it must at a minimum ensure that the conditions in the proposed Order ''are applied with full force and without exceptions or dilution.'' [403] UK EMIR article 11(2) would require the Covered Entity to mark-to-market or mark-to-model its non–centrally cleared contracts. Other UK portfolio reconciliation requirements contemplate that counterparties will use this valuation as an input to the reconciliation process. For example, a portfolio reconciliation must include at least the valuation attributed to each contract in accordance with UK EMIR article 11(2).[404] As UK EMIR article 11(2) sets the standards under which a Covered Entity must calculate this key input in the portfolio reconciliation process, the Commission has determined that this provision is related to portfolio reconciliation and accordingly is retaining the Order's reference to it.[405]

7. Clearing Rights Disclosure

Because UK clearing provisions do not require disclosure of a counterparty's clearing rights under Exchange Act section 3C(g)(5), the Commission views those provisions as not comparable to Exchange Act clearing rights disclosure requirements. Commenters did not address this conclusion and, consistent with the proposed Order, the Commission is not providing substituted compliance.

VIII. Substituted Compliance for Recordkeeping, Reporting and Notification Requirements

A. Proposed Approach

The FCA Application in part requested substituted compliance for requirements applicable to SBS Entities under the Exchange Act relating to:

- *Record Making*—Exchange Act rule 18a–5 requires prescribed records to be made and kept current.[406]
- *Record Preservation*—Exchange Act rule 18a–6 requires preservation of records.[407]
- *Reporting*—Exchange Act rule 18a–7 requires certain reports.[408]
- *Notification*—Exchange Act rule 18a–8 requires notification to the Commission when certain financial or operational problems occur.[409]
- *Securities Count*—Exchange Act rule 18a–9 requires non-prudentially regulated security-based swap dealers to perform a quarterly securities count.[410]
- *Daily Trading Records.* Exchange Act section 15F(g) requires SBS Entities to maintain daily trading records.[411]

Taken as a whole, the recordkeeping, reporting, notification, and securities count requirements that apply to SBS Entities are designed to promote the prudent operation of the firm's security-based swap activities, assist the Commission in conducting compliance examinations of those activities, and alert the Commission to potential financial or operational problems that could impact the firm and its customers.[412]

In proposing to provide conditional substituted compliance in connection with this part of the FCA Application, the Commission preliminarily concluded that the relevant UK requirements, subject to conditions and limitations, would produce regulatory outcomes that are comparable to the outcomes associated with the vast majority of the recordkeeping, reporting, notification, and securities count requirements under the Exchange Act applicable to SBS Entities pursuant to

[402] *See* SIFMA 5/3/2021 Letter at 21 and Appendix A part (e)(6).

[403] *See* Better Markets Letter at 2.

[404] *See* UK EMIR article 13(2).

[405] *See* para. (e)(6) of the Order.

[406] *See* 17 CFR 240.18a–5. The FCA Application discusses UK requirements that address firms' record creation obligations related to matters such as financial condition, operations, transactions, counterparties, and their property, personnel, and business conduct. *See* FCA Application Appendix B category 2 at 101–28, 136–39.

[407] *See* 17 CFR 240.18a–6. The FCA Application discusses UK requirements that address firms' record preservation obligations related to records that firms are required to create, as well as additional records such as records of communications. *See* FCA Application Appendix B category 2 at 140–71.

[408] *See* 17 CFR 240.18a–7. The FCA Application discusses UK requirements that address firms' obligations to make certain reports. *See* FCA Application Appendix B category 2 at 172–80, 185–89.

[409] *See* 17 CFR 240.18a–8. The FCA Application discusses UK requirements that address firms' obligations to make certain notifications. *See* FCA Application Appendix B category 2 at 181–85.

[410] *See* 17 CFR 240.18a–9. The FCA Application discusses UK requirements that address firms' obligations to perform securities counts. *See* FCA Application Appendix B category 2 at 129–36.

[411] *See* 15 U.S.C. 78*o*–10(g). The FCA Application discusses UK requirements that address firms' record preservation obligations related to records that firms are required to create, as well as additional records such as records of communications. *See* FCA Application Appendix B category 2 at 140–71.

[412] Rule 3a71–6 sets forth additional analytic considerations in connection with substituted compliance for the Commission's recordkeeping, reporting, notification, and securities count requirements. In particular, Exchange Act rule 3a71–6(d)(6) provides that the Commission intends to consider (in addition to any conditions imposed) ''whether the foreign financial regulatory system's required records and reports, the timeframes for recording or reporting information, the accounting standards governing the records and reports, and the required format of the records and reports'' are comparable to applicable provisions under the Exchange Act, and whether the foreign provisions ''would permit the Commission to examine and inspect regulated firms' compliance with the applicable securities laws.''

Exchange Act rules 18a–5, 18a–6, 18a–7, 18a–8, and 18a–9 and Exchange Act section 15F(g) (collectively, the ''Exchange Act Recordkeeping and Reporting Requirements'').[413]

Finally, the proposed structure of the substituted compliance determinations with respect to Exchange Act rules 18a–5, 18a–6, 18a–7, 18a–8, and 18a–9, as well as Exchange Act Section 15F(g) would have permitted a covered entity to apply substituted compliance with respect to certain of these rules (*e.g.,* Exchange Act rules 18a–5 and 18a–6) and comply with the Exchange Act requirements of the remaining rules and statute (*i.e.,* Exchange Act rules 18a–7, 18a–8, and 18a–9, as well as Exchange Act Section 15F(g)).[414] Moreover, the proposed structure of the substituted compliance determinations with respect to the recordkeeping rules would have provided Covered Entities with greater flexibility to select distinct requirements within the broader rules for which they want to apply substituted compliance.

Because the Exchange Act Recordkeeping and Reporting Requirements were entity-level requirements, the Covered Entity needed to apply substituted compliance at the entity level for each of the substituted compliance determinations with respect to these requirements with one limited exception. Under the exception, a Covered Entity could apply substituted compliance at the transaction level with respect to requirements in Exchange Act rules 18a–5 and 18a–6 linked to counterparty protection rules (*i.e.,* Exchange Act rules 15Fh–3(b), (c), (e), (f), and (g)).

B. Commenter Views and Final Provisions

1. General Considerations

The Commission structured its preliminary substituted compliance determinations in the proposed Order with respect to Exchange Act rules 18a–5, 18a–6, 18a–7, and 18a–8 to provide Covered Entities with greater flexibility to select which distinct requirements within the broader rules for which they want to apply substituted compliance.[415] This flexibility was intended to permit Covered Entities to leverage existing recordkeeping and reporting systems that are designed to comply with the broker-dealer recordkeeping and reporting requirements on which the recordkeeping and reporting requirements applicable to SBS Entities are based. For example, it may be more efficient for a Covered Entity to comply with certain Exchange Act requirements within a given recordkeeping or reporting rule (rather than apply substituted compliance) because it can utilize systems that its affiliated broker-dealer has implemented to comply with them.

As applied to Exchange Act rules 18a–5 and 18a–6, this approach of providing greater flexibility resulted in preliminary substituted compliance determinations with respect to the different categories of records these rules require SBS Entities to make, keep current, and/or preserve. The objectives of these rules—taken as a whole—is to assist the Commission in monitoring and examining for compliance with Exchange Act requirements applicable to SBS Entities as well as to promote the prudent operation of these firms.[416] The Commission preliminarily found that the comparable UK recordkeeping rules achieve these outcomes with respect to compliance with the substantive UK requirements for which preliminary positive substituted compliance determinations were made (*e.g.,* capital and margin requirements). At the same time, the recordkeeping rules address different categories of records through distinct requirements within the rules. Each requirement with respect to a specific category of records (*e.g.,* paragraph (a)(2) of Exchange Act rule 18a–5 addressing ledgers (or other records) reflecting all assets and liabilities, income and expense, and capital accounts) can be viewed in isolation as a distinct recordkeeping rule. Therefore, the Commission preliminarily found it appropriate to make substituted compliance determinations at this level of Exchange Act rules 18a–5 and 18a–6.

A commenter generally supported the Commission's proposed granular approach to making substituted compliance determinations.[417] The Order implements this granular approach substantially as proposed.

The Commission's preliminary substituted compliance determinations for the Exchange Act Recordkeeping and Reporting Requirements were subject to the condition that the Covered Entity is subject to and complies with the relevant UK laws.[418] Further, the Commission proposed limitations and additional conditions for certain of the proposed preliminary substituted compliance determinations. The limitations and conditions are discussed below as well any comments on them and the Commission's response to those comments.

First, the Commission did not make a preliminary positive substituted compliance determination with respect to a discrete provision of the Exchange Act Recordkeeping and Reporting Requirements if it was fully or partially linked to a substantive Exchange Act requirement for which substituted compliance was not available or for which a preliminary positive substituted compliance determination was not being made.[419] In this regard, the Commission linked a requirement in Exchange Act rule 18a–5 to Exchange Act rule 10b–10.[420] A commenter pointed out that Covered Entities will not be subject to Exchange Act rule 10b–10.[421] The Commission agrees with the commenter that there are no provisions in the Exchange Act Recordkeeping and Reporting Requirements that are linked to Exchange Act rule 10b–10. Consequently, the Order does not contain this exclusion.

In addition, Exchange Act rule 18a–6(c), in part, requires firms to preserve Forms SBSE, SBSE–A, SBSE–C, SBSE–W, all amendments to these forms, and all other licenses or other documentation showing the firm's registration with any securities regulatory authority or the U.S. Commodity Futures Trading Commission. Because these requirements are linked to the Commission's and other U.S. regulators' registration rules, for which substituted compliance is not granted, the Order excludes the requirement to preserve these records from the Commission's positive substituted compliance determination with respect to Exchange Act rule 18a–6(c).[422]

Aside from these modifications, the Order does not extend substituted compliance to discrete Exchange Act Recordkeeping and Reporting Requirements that are linked to substantive Exchange Act requirements for which there is no substituted compliance, as proposed. In particular, a positive substituted compliance determination is not being made, in full or in part, for recordkeeping, reporting, or notification requirements linked to

[413] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18394–404, 18415–20.

[414] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18395–96.

[415] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18394–404, 18415–20.

[416] *See, e.g.,* Exchange Act Release No. 71958 (Apr. 17, 2014), 79 FR 25194, 25199–200 (May 2, 2014).

[417] *See* SIFMA 5/3/2021 Letter at 21–23.

[418] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18394–404, 18415–20.

[419] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18395 (discussing this limitation).

[420] 17 CFR 240.10b–10.

[421] *See* SIFMA 5/3/2021 Letter at 22–23.

[422] *See* para. (f)(2)(i)(L) of the Order.

the following Exchange Act rules for which substituted compliance is not available or a positive substituted compliance determination is not being made: (1) Exchange Act rule 15Fh–4;[423] (2) Exchange Act rule 15Fh–5;[424] (3) Exchange Act rule 15Fh–6;[425] (4) Exchange Act rule 18a–2;[426] (5) Exchange Act rule 18a–4; and (6) Regulation SBSR.[427]

Second, the Commission did not make a positive substituted compliance determination with respect to the inspection requirement of Exchange Act section 15F(f) and the records production requirement of Exchange Act rule 18a–6(g).[428] The Commission did not receive comment on this approach and the Order does not extend substituted compliance to these requirements.

Third, the Commission conditioned substituted compliance with discrete provisions of the Exchange Act Recordkeeping and Reporting Requirements that were fully or partially linked to a substantive Exchange Act requirement for which substituted compliance was available on the Covered Entity applying substituted compliance with respect to the linked Exchange Act requirement.[429] In particular, substituted compliance for a provision of the Exchange Act Recordkeeping and Reporting Requirements that is linked to the following Exchange Act rules was conditioned on the SBS Entity applying substituted compliance to the linked substantive Exchange Act rule: (1) Exchange Act rule 15Fh–3, except paragraphs (a) and (d) of the rule for which substituted compliance is not available; (2) Exchange Act rule 15Fi–2; (3) Exchange Act rule 15Fi–3; (4) Exchange Act rule 15Fi–4; (5) Exchange Act rule 15Fi–5; (6) Exchange Act rule 15Fk–1; (7) Exchange Act rule 18a–1 (''Rule 18a–1 Condition''); (8) Exchange Act rule 18a–3; (8) Exchange Act rule 18a–5; and (9) Exchange Act rule 18a–7. The Commission did not receive comment on this approach and is adopting it as proposed.

The only difference is that the positive substituted compliance determination for Exchange Act rule 18a–6(b)(1)(viii) is now conditioned on the Covered Entity applying substituted compliance for the requirements of Exchange Act rule 18a–7(a)(1), (b), and (c) through (h), and Exchange Act rule 18a–7(j) as applied to these requirements, rather than on the entirety of Exchange Act rule 18a–7, to reflect that substituted compliance with respect to Exchange Act rule 18a–7 is granted on a paragraph-by-paragraph basis and not all paragraphs of Exchange Act rule 18a–7 are pertinent to Exchange Act rule 18a–6(b)(1)(viii).

Moreover, for the reasons discussed above in part III.B.2.k. of this release, substituted compliance with respect to paragraphs (a)(1), (b), and (c) through (h) of Exchange Act rule 18a–7 is subject to the additional condition that the Covered Entity applies substituted compliance with respect to Exchange Act rule 18a–6(b)(1)(viii) (a record preservation requirement).[430] This record preservation requirement is directly linked to the financial and operational reporting requirements of paragraphs (a)(1), (b), and (c) through (h) of Exchange Act rule 18a–7. The proposed Order conditioned substituted compliance with respect to this record preservation requirement on the Covered Entity applying substituted compliance with respect to Exchange Act rule 18a–7(a)(1).[431] This additional condition is designed to provide clarity as to the Covered Entity's obligations under this record preservation requirement when applying substituted compliance with respect to paragraphs (a)(1), (b), and (c) through (h) of Exchange Act rule 18a–7 pursuant this Order.

Fourth, the Commission conditioned substituted compliance with discrete provisions of the Exchange Act Recordkeeping and Reporting Requirements that would be important for monitoring or examining compliance with the capital rule for nonbank security-based swap dealers on the Covered Entity applying substituted compliance with respect to the capital rule (*i.e.,* the Rule 18a–1 Condition).[432] The Commission included the Rule 18a–1 Condition as part of the substituted compliance determination for the daily trading records requirement of Exchange Act section 15F(g). A commenter asked that the condition be modified so that it applies only if the Covered Entity is not prudentially regulated (and therefore subject to rule 18a–1).[433] Instead, the Commission is deleting this condition from the substituted compliance determination because these requirements are not important to monitoring or examining for compliance with Exchange Act rule 18a–1. Therefore, all Covered Entities—whether or not subject to rule 18a–1—can apply substituted compliance with respect to Exchange Act section 15F(g). The Order otherwise includes the Rule 18a–1 Condition for discrete provisions of the Exchange Act Recordkeeping and Reporting Requirements that would be important for monitoring or examining compliance with the capital rule for nonbank security-based swap dealers, as proposed.

Fifth, the proposed Order included a condition that Covered Entities must promptly furnish to a representative of the Commission upon request an English translation of any record, report, or notification of the Covered Entity that is required to be made, preserved, filed, or subject to examination pursuant to Exchange Act section 15F of this Order.[434] The Commission did not receive a comment on this approach and the Order includes this condition.

Sixth, the Commission conditioned substituted compliance with Exchange Act rule 18a–7 on Covered Entities filing periodic unaudited financial and operational information with the Commission or its designee in the manner and format required by Commission rule or order. Commenters made new suggestions about the scope and requirements of such a Commission order or rule in addition to reiterating comments previously made in response to the same condition in the German Substituted Compliance Order.[435] First, if SBS Entities are required to prepare FOCUS Report Part II, and a positive substituted compliance determination is made with respect to the Commission's capital requirements, a commenter proposed that the Commission permit a Covered Entity to submit capital computations in a manner consistent with its home country capital standards and related reporting rules.[436] Second, some commenters asked that Covered Entities be permitted to file their unaudited financial information less frequently (*e.g.,* quarterly) and provide a later submission deadline to match the frequency of reporting and reporting deadlines required by the Covered

[423] 17 CFR 240.15Fh–4.

[424] 17 CFR 240.15Fh–5.

[425] 17 CFR 240.15Fh–6.

[426] 17 CFR 240.18a–2.

[427] 17 CFR 242.900 *et seq.*

[428] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18403–404 (discussing this condition).

[429] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18395 (discussing this condition).

[430] *See* para. (f)(3)(i)(D) of the Order.

[431] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18399, 18417.

[432] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18395 (discussing this condition).

[433] *See* SIFMA 5/3/2021 Letter at 23.

[434] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18395 (discussing this condition).

[435] *See* SIFMA 5/3/2021 Letter Appendix B.

[436] *See* SIFMA 5/3/2021 Letter Appendix B.

Entity's home country regulator,[437] while other commenters urged that Covered Entities be subject to monthly instead of quarterly reporting of their financial condition.[438] Third, commenters supported a potential approach identified by the Commission under which Covered Entities would be permitted to satisfy their Exchange Act rule 18a–7 obligations for a two-year period by filing the FOCUS Report Part IIC with only a limited number of the required line items completed.[439] Fourth, the Commission received comment recommending that the FOCUS Report be modified to omit certain line items either permanently or during a two-year transition.[440] The Commission will consider these comments as it works towards completing a Commission order or rule pursuant to the provision in this Order that substituted compliance with respect to Exchange Act rule 18a–7's FOCUS Report filing requirements is conditioned on Covered Entities filing unaudited financial and operational information in the manner and format specified by Commission order or rule.

Seventh, the Commission proposed to make a positive substituted compliance determination with respect to Exchange Act rule 18a–6(b)(2)(v) but not with respect to Exchange Act rule 18a–6(b)(1)(viii)(L), even though both provisions require firms to preserve detail relating to information for possession or control requirements under Exchange Act rule 18a–4 and reported on Part II of Form X–17A–5. These provisions are fully linked with Exchange Act rule 18a–4 for which a positive substituted compliance is not available, so a positive substituted compliance determination should not be made for these linked record retention requirements. Accordingly, the Order does not make a positive substituted compliance determination with respect to Exchange Act rule 18a–6(b)(2)(v).

The Commission also received comment suggesting certain modifications to the ordering language. Specifically, a commenter suggested revising paragraph (f)(4)(ii)(A)(*1*) of the proposed Order, which requires a Covered Entity to send a copy of any notice required to be sent by UK laws cited in paragraph (f)(4) simultaneously to the Commission. The commenter recommended revising this provision to require the notices that a Covered Entity would be required to send to the Commission be limited to those notices required by UK law cited in paragraph (f)(4)(i)(C) only instead of paragraph (f)(4). Furthermore, the commenter recommended conditioning the requirement to provide these notices to the Commission to be limited to those notifications that are related to: (1) A breach of the UK laws cited in the relevant portions of paragraphs (f)(1) or (2) of the Order, which, in the case of a Covered Entity that is prudentially regulated, also relates to the Covered Entity's business as a security-based swap dealer or major security-based swap participant; or (2) a deficiency relating to capital requirements.[441] The commenter reasoned that the provisions of UK law requiring notification referenced in paragraph (f)(4) require notification of a far wider array of matters than those described in Exchange Act rule 18a–8.

The Commission disagrees. Exchange Act rule 18a–8 requires security-based swap dealers and major security-based swap participants for which there is no prudential regulator to notify the Commission of a failure to meet minimum net capital. Exchange Act rule 18a–8 also specifies several events that trigger a requirement that a security-based swap dealer or major security-based swap participant for which there is no prudential regulator must send notice within twenty-four hours to the Commission. These notices are designed to provide the Commission with ''early warning'' that the SBS entity may experience financial difficulty. Furthermore, Exchange Act rule 18a–8 requires bank security-based swap dealers to give notice to the Commission when it files an adjustment of its reported capital category with its prudential regulator. Additional notification requirements arise with respect to the failure to maintain and keep current required books and records, the discovery of material weaknesses, and failure to make a required deposit into the special reserve account for the exclusive benefit of security-bases swap customers.[442] While the specific UK requirements cited with respect to Exchange Act rule 18a–8 are different from the specific requirements set forth in Exchange Act rule 18a–8, the Commission believes the UK notice requirements cited in paragraph (f)(4) of the Order provide for comparable regulatory outcomes by requiring notification of events or conditions which may impact an SBS Entity's capital or signal the potential for financial difficulty, indicate the failure to maintain and keep current books and records, or the potential for the failure to comply with other requirements related to the protection of customer assets. The recommended revisions would reduce the scope of notifications the Commission would receive. Consequently, the Commission is not making the recommended revisions with respect to paragraph (f)(4)(ii)(A)(*1*).

The commenter also recommended revising paragraphs (f)(2)(i)(H)(*1*), (f)(3)(i)(A), and (f)(3)(ii)(A) to include the qualifier ''as applicable'' with respect to citations to UK CRR Reporting ITS annexes. The commenter stated that not all firms submit all of the UK CRR Reporting ITS annexes.[443] Accordingly, the Commission is modifying these paragraphs to include the qualifier ''as applicable.''[444]

Finally, with respect to recordkeeping rules that are linked with Exchange Act rule 15Fh–3, references to Exchange Act rule 15Fh–3 are revised to clarify that substituted compliance is available with respect to Exchange Act rule 15Fh–3 except paragraphs (a) and (d) of the rule, instead of the entirety of Exchange Act rule 15Fh–3. Accordingly, the Commission is revising the conditions in paragraphs (f)(1)(i)(M)(*2*) and (f)(2)(i)(K)(*2*) of the Order to state that the Covered Entity must apply substituted compliance with respect to the portion of the recordkeeping rule that relates to ''one or more provisions of Exchange Act rule 15Fh–3 for which substituted compliance is available under this Order'' (instead of just ''Exchange Act rule 15Fh–3'').

2. Citations to UK Law

The Commission also received comment recommending changes to the proposed Order to refine the scope of UK law provisions that would operate as conditions to substituted compliance.[445] The Commission reviewed each of the UK law citations that the commenter recommended adding or removing from the Order for relevance to the comparable Exchange Act requirement while also keeping in mind that each UK law citation was included in the FCA Application intentionally. The Commission's conclusion and reasoning with respect to the commenter's recommendations is discussed in further detail below. In addition to refining the scope of UK law citations in response to comment, the

[437] *See* SIFMA 5/3/2021 Letter Appendix B.

[438] *See* Americans for Financial Reform Education Fund Letter at 1.

[439] *See* SIFMA 5/3/2021 Letter Appendix B.

[440] *See* SIFMA 5/3/2021 Letter Appendix B.

[441] *See* SIFMA 5/3/2021 Letter Appendix A.

[442] *See* 17 CFR 240.18a–8.

[443] *See* SIFMA 5/3/2021 Letter Appendix A.

[444] *Compare* paras. (f)(2)(i)(H)(*1*), (f)(3)(i)(A), and (f)(3)(ii)(A) of the UK Substituted Compliance Notice and Proposed Order, *with* paras. (f)(2)(i)(H)(*1*), (f)(3)(i)(A), and (f)(3)(ii)(A) of the Order.

[445] *See* SIFMA 5/3/2021 Letter Appendix A.

Order reflects changes to the UK law citations after refining the UK law provisions in the proposed Order to better reflect the UK law provisions cited in the FCA Application, as well as the EU law provisions cited in the French Substituted Compliance Order.[446]

a. Global

The commenter recommended deleting references to UK MiFID Org Reg, COBS 8A, and UK MiFIR article 25(1), reasoning that these provisions could raise issues due to the discrepancy between Exchange Act requirements, which apply on an entity-level basis, and these UK requirements, which are territorially limited. As explained in part III.B.2. above, conducting business outside the UK does not preclude a firm from relying on substituted compliance for the business it conducts within the UK. Accordingly, other than the specific articles of UK MiFID Org Reg, FCA COBS, and UK MiFIR discussed below, the Commission is not removing references to these UK requirements from the Order's list of UK requirements comparable to the Commission's recordkeeping, reporting, notification, and securities count requirements.

The commenter recommended deleting references to FCA IFPRU, reasoning that FCA IFPRU does not apply to banks and PRA-designated investment firms, and all Covered Entities are expected to be banks or PRA-designated investment firms. On further examination, the Commission believes that the IFPRU provisions are not necessary to find comparability with respect to the Commission's recordkeeping, reporting, notification, and securities count requirements and is therefore removing references to this UK requirement.[447]

The commenter recommended deleting references to FCA COBS 9A.2.1R, which relates to suitability requirements, reasoning that the provision does not correspond to, and goes beyond, the Commission's recordkeeping, reporting, notification, and securities count requirements. The Commission agrees with the commenter's reasoning, except with respect to Exchange Act rules 18a–5(a)(17) and (b)(13), which relate to suitability records, and is therefore removing references to this UK requirement from the Order's list of UK requirements comparable to the Commission's recordkeeping, reporting, notification, and securities count requirements, except for Exchange Act rules 18a–5(a)(17) and (b)(13).[448]

The commenter recommended deleting references to UK MiFID Org Reg article 76 and FCA SYSC 10A.1.6R and 10A.1.8R, which relate to the recording of telephone and electronic communications, reasoning that they do not correspond to, and go beyond, the requirements of the Commission's recordkeeping, reporting, notification, and securities count rules. The Commission agrees with the commenter's reasoning, except with respect to Exchange Act rules 18a–6(b)(1)(iv) and (b)(2)(ii), which relate to communications including telephonic communications. Therefore, the Commission is removing references to these UK requirements from the Order's list of UK requirements comparable to the Commission's recordkeeping, reporting, notification, and securities count requirements, except for Exchange Act rules 18a–6(b)(1)(iv) and (b)(2)(ii).[449]

The commenter recommended deleting references to FCA FCG, reasoning that this sourcebook only contains nonbinding guidance. The Commission agrees with the commenter's reasoning and is therefore removing references to this UK requirement from the Order's list of UK requirements comparable to the Commission's recordkeeping, reporting, notification, and securities count requirements.[450]

The commenter recommended deleting references to FCA FIT, reasoning that FCA FIT only contains nonbinding guidance. The Commission agrees with the commenter's reasoning and is therefore removing references to this UK requirement from the Order's list of UK requirements comparable to the Commission's recordkeeping, reporting, notification, and securities count requirements.[451]

The commenter recommended deleting references to the EBA Guidelines on Outsourcing, reasoning that they only contain nonbinding guidance. The Commission agrees with the commenter's reasoning and is therefore removing references to this UK requirement from the Order's list of UK requirements comparable to the Commission's recordkeeping, reporting, notification, and securities count requirements.[452]

In addition, the Commission is deleting references to FCA provisions ending in ''G'', because they only contain nonbinding guidance.[453] Therefore, these UK requirements are removed from the Order's list of UK requirements comparable to the Commission's recordkeeping, reporting, notification, and securities count requirements.[454]

b. Exchange Act Rules 18a–5 and 18a–6

The commenter recommended deleting references to UK MiFIR article 25(1), which sets a duration of five years for firms to keep relevant data relating to orders and transactions in financial instruments, reasoning that this does

[446] There are a number of subparagraphs of the recordkeeping, reporting, notification, and securities count paragraph of the Order that reflect changes for consistency with the FCA Application and French Substituted Compliance Order. *Compare* paras. (f)(1)(i)(B)(*1*), (f)(1)(i)(C)(*1*), (f)(1)(i)(D)(*1*), (f)(1)(i)(F)(*1*), (f)(1)(i)(G)(*1*), (f)(1)(i)(H)(*1*), (f)(1)(i)(I)(*1*), (f)(1)(i)(J)(*1*), (f)(1)(i)(K), (f)(1)(i)(L)(*1*), (f)(2)(i)(A), (f)(2)(i)(B), (f)(2)(i)(C)(*1*), (f)(2)(i)(D), (f)(2)(i)(E)(*1*), (f)(2)(i)(F)(*1*), (f)(2)(i)(G)(*1*), (f)(2)(i)(H)(*1*), (f)(2)(i)(I)(*1*), (f)(2)(i)(J)(*1*), (f)(2)(i)(K)(*1*), (f)(2)(i)(L), (f)(2)(i)(M), (f)(2)(i)(N)(*1*), (f)(2)(i)(O)(*1*), (f)(2)(i)(P)(*1*), (f)(2)(i)(Q), (f)(2)(i)(R), (f)(3)(ii)(A), (f)(3)(iii), (f)(3)(iv)(A), (f)(4)(i)(A)(*1*), (f)(4)(i)(B), (f)(4)(i)(C)(*1*), and (f)(4)(i)(D)(*1*) of the UK Substituted Compliance Notice and Proposed Order, *with* paras. (f)(1)(i)(B)(*1*), (f)(1)(i)(C)(*1*), (f)(1)(i)(D)(*1*), (f)(1)(i)(F)(*1*), (f)(1)(i)(G)(*1*), (f)(1)(i)(H)(*1*), (f)(1)(i)(I)(*1*), (f)(1)(i)(J)(*1*), (f)(1)(i)(K), (f)(1)(i)(L)(*1*), (f)(2)(i)(A), (f)(2)(i)(B), (f)(2)(i)(C)(*1*), (f)(2)(i)(D), (f)(2)(i)(E)(*1*), (f)(2)(i)(F)(*1*), (f)(2)(i)(G)(*1*), (f)(2)(i)(H)(*1*), (f)(2)(i)(I)(*1*), (f)(2)(i)(J)(*1*), (f)(2)(i)(K)(*1*), (f)(2)(i)(L)(*1*), (f)(2)(i)(M), (f)(2)(i)(N)(*1*), (f)(2)(i)(O)(*1*), (f)(2)(i)(P)(*1*), (f)(2)(i)(Q), (f)(2)(i)(R), (f)(3)(ii)(A), (f)(3)(iii), (f)(3)(iv)(A), (f)(4)(i)(A)(*1*), (f)(4)(i)(B), (f)(4)(i)(C)(*1*), (f)(4)(i)(D)(*1*), and (f)(6) of the Order.

[447] *Compare* paras. (f)(1)(i)(B)(*1*), (f)(1)(i)(J)(*1*), (f)(1)(i)(L)(*1*), (f)(2)(i)(A), (f)(2)(i)(B), (f)(2)(i)(C)(*1*), (f)(2)(i)(D), (f)(2)(i)(I)(*1*), (f)(2)(i)(J)(*1*), (f)(4)(i)(A)(*1*), (f)(4)(i)(B), (f)(4)(i)(C)(*1*), and (f)(4)(i)(D)(*1*) of the UK Substituted Compliance Notice and Proposed Order, *with* paras. (f)(1)(i)(B)(*1*), (f)(1)(i)(J)(*1*), (f)(1)(i)(L)(*1*), (f)(2)(i)(A), (f)(2)(i)(B), (f)(2)(i)(C)(*1*), (f)(2)(i)(D), (f)(2)(i)(I)(*1*), (f)(2)(i)(J)(*1*), (f)(4)(i)(A)(*1*), (f)(4)(i)(B), and (f)(4)(i)(C)(*1*) of the Order.

[448] *Compare* paras. (f)(1)(i)(D)(*1*), (f)(1)(i)(G)(*1*), (f)(1)(i)(I)(*1*), (f)(2)(i)(A), (f)(2)(i)(B), and (f)(2)(i)(D) of the UK Substituted Compliance Notice and Proposed Order, *with* paras. (f)(1)(i)(D)(*1*), (f)(1)(i)(G)(*1*), (f)(1)(i)(I)(*1*), (f)(2)(i)(A), (f)(2)(i)(B), and (f)(2)(i)(D) of the Order.

[449] *Compare* paras. (f)(1)(i)(A)(*1*), (f)(1)(i)(D)(*1*), (f)(1)(i)(F)(*1*), (f)(1)(i)(G)(*1*), (f)(1)(i)(I)(*1*), (f)(1)(i)(M), (f)(2)(i)(A), (f)(2)(i)(B), and (f)(2)(i)(O)(i) of the UK Substituted Compliance Notice and Proposed Order, *with* paras. (f)(1)(i)(A)(*1*), (f)(1)(i)(D)(*1*), (f)(1)(i)(F)(*1*), (f)(1)(i)(G)(*1*), (f)(1)(i)(I)(*1*), (f)(1)(i)(M), (f)(2)(i)(A), (f)(2)(i)(B), and (f)(2)(i)(O)(i) of the Order.

[450] *Compare* paras. (f)(1)(i)(B)(*1*), (f)(1)(i)(J)(*1*), (f)(1)(i)(L)(*1*), (f)(2)(i)(A), (f)(2)(i)(B), and (f)(2)(i)(D) of the UK Substituted Compliance Notice and Proposed Order, *with* paras. (f)(1)(i)(B)(*1*), (f)(1)(i)(J)(*1*), (f)(1)(i)(L)(*1*), (f)(2)(i)(A), (f)(2)(i)(B), and (f)(2)(i)(D) of the Order.

[451] *Compare* paras. (f)(1)(i)(K) and (f)(2)(i)(M) of the UK Substituted Compliance Notice and Proposed Order, *with* paras. (f)(1)(i)(K) and (f)(2)(i)(M) of the Order.

[452] *Compare* para. (f)(2)(i)(R) of the UK Substituted Compliance Notice and Proposed Order, *with* para. (f)(2)(i)(R) of the Order.

[453] *See* FCA Reader's Guide: An Introduction to the Handbook (Jan. 2019), available at: *https://www.fca.org.uk/publication/handbook/readers-guide_0.pdf.*

[454] *Compare* para. (f)(2)(i)(R) of the UK Substituted Compliance Notice and Proposed Order, *with* para. (f)(2)(i)(R) of the Order.

not correspond to, and goes beyond, the requirements of Exchange Act rules 18a–5 and 18a–6. With respect to Exchange Act rule 18a–6, the five year record retention period is directly relevant to the record preservation requirement in Exchange Act rule 18a–6. With respect to Exchange Act rule 18a–5, while this UK requirement contains a record retention element, it also contains a record creation requirement that is relevant to Exchange Act rule 18a–5. Accordingly, the Commission is not removing references to this UK requirement from the Order's list of UK requirements comparable to Exchange Act rules 18a–5 and 18a–6.

The commenter recommended deleting references to PRA Internal Capital Adequacy Assessment Rules, which relate to a firm's distribution of financial resources, own funds and internal capital, and related risk management processes, reasoning that they do not correspond to, and go beyond, the requirements of Exchange Act rules 18a–5 and 18a–6. While the rules require firms to implement ''strategies, processes and systems'', the FCA Application states that in practice, one or more of these provisions ''will require the maintenance of full records of the Investment Firm's assets, liabilities, income and expense and capital accounts to be maintained'' which is relevant to Exchange Act rules 18a–5 and 18a–6.[455] Accordingly, the Commission is not removing references to these UK requirements from the Order's list of UK requirements comparable to Exchange Act rules 18a–5 and 18a–6, except with respect to Exchange Act rules 18a–6(b)(1)(iv) and (b)(2)(ii) for which the Commission agrees with the commenter's reasoning.[456]

The commenter recommended deleting references to certain parts of FCA CASS, which relate to a firm's holding of safe custody assets and client money, reasoning that this does not correspond to, and goes beyond, the requirements of Exchange Act rules 18a–5 and 18a–6. However, the FCA Application states that, among other things, these provisions require firms to ''maintain detailed, up-to-date and accurate accounts and records distinguishing client money and assets from those of the Investment Firm,'' which is relevant to Exchange Act rules 18a–5 and 18a–6.[457] Accordingly, the Commission is not removing references to these UK requirements from the Order's list of UK requirements comparable to Exchange Act rules 18a–5 and 18a–6, except with respect to Exchange Act rule 18a–5(a)(12) and Exchange Act rules 18a–6(b)(1)(iv) and (b)(2)(ii) for which the Commission agrees with the commenter's reasoning.[458]

The commenter recommended deleting references to UK EMIR article 11, which relates to the timely confirmation of transactions, and UK EMIR article 39, which relates to a firm's requirement to segregate the positions they clear for a client with a UK central counterparty from their own positions, reasoning that they do not correspond to, and go beyond, the requirements of Exchange Act rules 18a–5 and 18a–6. While these UK requirements contain segregation and confirmation requirements, they also contain record creation requirements that are relevant to Exchange Act rule 18a–5. Accordingly, the Commission is not removing references to these UK requirements from the Order's list of UK requirements comparable to Exchange Act rule 18a–5, except with respect to Exchange Act rule 18a–5(a)(12) for which the Commission agrees with the commenter's reasoning.[459] However, the Commission agrees with the commenter's reasoning with respect to Exchange Act rule 18a–6 and is removing references to these UK requirements from the Order's list of UK requirements comparable to Exchange Act rule 18a–6.[460]

The commenter recommended deleting references to UK CRR articles 103, 105(3), and 105(10), which relate to the firm's management of trading book exposures, reasoning that they do not correspond to, and go beyond, the requirements of Exchange Act rules 18a–5 and 18a–6. However, the FCA Application states that these requirements in practice require firms to have ''a record of their long and short positions to enable these to be monitored'' which is relevant to Exchange Act rules 18a–5 and 18a–6.[461] Accordingly, the Commission is not removing references to these UK requirements from the Order's list of UK requirements comparable to Exchange Act rules 18a–5 and 18a–6.

The commenter recommended deleting references to UK CRR article 104(1)(j) from the Order, reasoning that the provision does not exist. The Commission agrees with the commenter's reasoning, and is therefore removing references to this citation from the Order's list of UK requirements comparable to Exchange Act rules 18a–5 and 18a–6.[462]

The commenter recommended deleting certain references to FCA COBS, which relate to client agreements for services and client reporting, reasoning that they do not correspond to, and go beyond, the requirements of Exchange Act rules 18a–5 and 18a–6. With respect to Exchange Act rule 18a–5, these provisions (other than FCA COBS 9A.2.1R which is discussed above) generally also contains record creation requirements that are relevant to Exchange Act rule 18a–5 and Exchange Act rules 18a–6(b)(1)(ix) and (d)(4) and (d)(5) (which implicate record creation). Accordingly, the Commission is not removing references to most of these UK requirements from the Order's list of UK requirements comparable to Exchange Act rule 18a–5 and Exchange Act rule 18a–6(b)(1)(ix), except for FCA COBS 8A.1.9R and 16A.2.1R with respect to Exchange Act rule 18a–5(a)(4), (a)(8), and (b)(3) for which the Commission agrees with the commenter's reasoning.[463] With respect to the remainder of Exchange Act rule 18a–6, the Commission is removing references to these UK requirements because FCA COBS is relevant to record creation but not record preservation.[464]

The commenter recommended deleting references to MLR 2017 Regulations 28 through 30, which relate to anti-money laundering customer due diligence measures, reasoning that they do not correspond to, and go beyond, the requirements of Exchange Act rules 18a–5 and 18a–6. These UK provisions contain record creation requirements regarding customers, but not record preservation requirements. Accordingly, the Commission is not removing

[455] *See* FCA Application at 109.

[456] *Compare* para. (f)(2)(i)(D) of the UK Substituted Compliance Notice and Proposed Order, with para. (f)(2)(i)(D) of the Order.

[457] *See* FCA Application at 110.

[458] *Compare* paras. (f)(1)(i)(L)(*1*) and (f)(2)(i)(D) of the UK Substituted Compliance Notice and Proposed Order, with paras. (f)(1)(i)(L)(*1*) and (f)(2)(i)(D) of the Order.

[459] *Compare* para. (f)(1)(i)(L)(*1*) of the UK Substituted Compliance Notice and Proposed Order, with para. (f)(1)(i)(L)(*1*) of the Order.

[460] *Compare* paras. (f)(2)(i)(A), (f)(2)(i)(B), (f)(2)(i)(C)(*1*), (f)(2)(i)(D), (f)(2)(i)(G)(*1*), (f)(2)(i)(I)(*1*), and (f)(2)(i)(O)(*1*) of the UK Substituted Compliance Notice and Proposed Order, *with* paras. (f)(2)(i)(A), (f)(2)(i)(B), (f)(2)(i)(C)(*1*), (f)(2)(i)(D), (f)(2)(i)(G)(*1*), (f)(2)(i)(I)(*1*), and (f)(2)(i)(O)(*1*) of the Order.

[461] *See* FCA Application at 111.

[462] *Compare* paras. (f)(2)(i)(E)(*1*) and (f)(2)(i)(H)(*1*) of the UK Substituted Compliance Notice and Proposed Order, *with* paras. (f)(2)(i)(E)(*1*) and (f)(2)(i)(H)(*i*) of the Order.

[463] *Compare* paras. (f)(1)(i)(D)(*1*) and (f)(1)(i)(I)(*1*) of the UK Substituted Compliance Notice and Proposed Order, *with* paras. (f)(1)(i)(D)(*1*) and (f)(1)(i)(I)(*1*) of the Order.

[464] *Compare* paras. (f)(2)(i)(A), (f)(2)(i)(B), (f)(2)(i)(D), (f)(2)(i)(F)(*1*), (f)(2)(i)(G)(*1*), and (f)(2)(i)(Q) of the UK Substituted Compliance Notice and Proposed Order, *with* paras. (f)(2)(i)(A), (f)(2)(i)(B), (f)(2)(i)(D), (f)(2)(i)(F)(*1*), (f)(2)(i)(G)(*1*), and (f)(2)(i)(Q) of the Order.

references to these UK requirements from the Order's list of UK requirements comparable to Exchange Act rule 18a–5 and Exchange Act rules 18a–6(b)(1)(xii) and (b)(2)(vii) (which implicate record creation), except with respect to Exchange Act rule 18a–5(a)(4), (a)(6), (a)(15), (b)(3), (b)(6), and (b)(11) for which the Commission agrees with the commenter's reasoning.[465] However, the Commission is removing references to these UK requirements from the Order's list of UK requirements comparable to the remainder of Exchange Act rule 18a–6.[466]

The commenter recommended deleting references to FCA COND at paragraphs 2C, 2D, 3B, 3C, 5D, and 5F, which set out certain minimum requirements for obtaining and maintaining PRA authorization, reasoning that they do not correspond to, and go beyond, the requirements of Exchange Act rules 18a–5 and 18a–6. However, the FCA Application states that these requirements effectively require firms to have ''systems and controls for maintaining records'' which is relevant to Exchange Act rules 18a–5 and 18a–6.[467] Accordingly, the Commission is not removing references to this UK requirement from the Order's list of UK requirements comparable to Exchange Act rules 18a–5 and 18a–6, except with respect to Exchange Act rule 18a–5(a)(6), (a)(8), (a)(15), (b)(6), and (b)(11) and Exchange Act rules 18a–6(b)(1)(iv) and (b)(2)(ii) for which the Commission agrees with the commenter's reasoning.[468]

The commenter recommended deleting references to PRA Fundamental Rules 2 and 6 and FCA PRIN 2.1.1R(2) and (3), which set out certain high-level principles for businesses, reasoning that they do not correspond to, and go beyond, the requirements of Exchange Act rules 18a–5 and 18a–6. However, the FCA Application states that, ''In practice, this will require UK firms to maintain adequate records and record-keeping systems.'' [469] Accordingly, the Commission is not removing references to these UK requirements from the Order's list of UK requirements comparable to Exchange Act rules 18a–5 and 18a–6, except with respect to Exchange Act rule 18a–5(a)(6), (a)(8), (a)(15), (b)(6), and (b)(11) and Exchange Act rules 18a–6(b)(1)(iv) and (b)(2)(ii) for which the Commission agrees with the commenter's reasoning.[470]

The commenter recommended deleting references to FSMA section 63(2A), which relates to the annual fit and proper reassessment requirement, and FSMA section 63F(5), which relates to the validity of a certificate issued to a firm's ''certification staff,'' and FSMA section 63(2A), which relates to the annual fit and proper reassessment requirement, reasoning that they do not correspond to, and go beyond, the requirements of Exchange Act rules 18a–5 and 18a–6. However, the FCA Application cites these provisions to support the statement that these certifications must be conducted annually,[471] and frequency of these certifications is relevant to Exchange Act rules 18a–5 and 18a–6. Accordingly, the Commission is not removing references to this UK requirement from the Order's list of UK requirements comparable to Exchange Act rules 18a–5 and 18a–6.

The commenter recommended deleting references to the PRA Certification Rules, the general PRA regime for certified employees, reasoning that they do not correspond to, and go beyond, the requirements of Exchange Act rules 18a–5 and 18a–6. The Commission agrees with the commenter's reasoning with respect to most of the PRA Certification Rules, but PRA Certification Rule 2.1 requires employees performing certification functions to have a valid certificate issued by the firm, which is relevant to Exchange Act rule 18a–5. Accordingly, the Commission is replacing references to the PRA Certification Rules with PRA Certification Rule 2.1 in the Order's list of UK requirements comparable to Exchange Act rules 18a–5 and 18a–6.[472]

The commenter recommended adding to paragraph (f)(1) of the Order regarding Exchange Act rule 18a–5 references to PRA Recordkeeping Rule 2.1 and FCA SYSC 9.1.1AR, which require firms to ''arrange for orderly records to be kept of its business and internal organization'', and to ''arrange for records to be kept of all services, activities, and transactions undertaken by it,'' respectively. The Commission agrees these UK requirements are relevant and is therefore adding them to the Order's list of UK requirements comparable to Exchange Act rule 18a–5.[473]

The commenter recommended deleting from paragraphs (f)(1) and (f)(2) of the Order references to UK MiFID Org Reg article 59, which set out the requirement to confirm execution of an order to the client, reasoning that it does not correspond to, and goes beyond, the requirements of Exchange Act rules 18a–5 and 18a–6. UK MiFID Org Reg article 59 identifies specific data elements that are relevant to the records required to be created under Exchange Act rule 18a–5, so the Commission is not removing references to this requirement from the Order's list of UK requirements comparable to Exchange Act rule 18a–5. However, the Commission agrees with the commenter's reasoning with respect to Exchange Act rule 18a–6 because UK MiFID Org Reg article 59 relates to record creation but not record preservation and is therefore removing references to this requirement from the Order's list of UK requirements comparable to Exchange Act rule 18a–6.[474]

The commenter recommended deleting from paragraphs (f)(1)(i)(K) and (f)(2)(i)(M) of the Order references to PRA General Organisational Requirements Rules 5.1 and 5.2, regarding management body requirements, reasoning that they do not correspond to, and go beyond, the requirements of Exchange Act rules 18a–5(a)(10) and (b)(8) (employment application record creation) and 18a–6(d)(1) (employment application record preservation). However, the FCA Application states that a ''CRR Firm's management body must define, oversee and be accountable for the implementation of the governance arrangements including, among other matters, ensuring the prevention of conflicts of interest'' (with respect to PRA General Organisational Requirement 5.1) and ''[e]ach member of the management body of a CRR Firm must be of sufficiently good repute and possess sufficient knowledge, skills and experience to perform their duties''

[465] *Compare* paras. (f)(1)(i)(D)(*1*) and (f)(1)(i)(G)(*1*) of the UK Substituted Compliance Notice and Proposed Order, *with* paras. (f)(1)(i)(D)(*1*) and (f)(1)(i)(G)(*1*) of the Order.

[466] *Compare* paras. (f)(2)(i)(A), (f)(2)(i)(B), and (f)(2)(i)(D) of the UK Substituted Compliance Notice and Proposed Order, *with* paras. (f)(2)(i)(A), (f)(2)(i)(B), and (f)(2)(i)(D) of the Order.

[467] *See* FCA Application at 126–27.

[468] *Compare* paras. (f)(1)(i)(G)(*1*), (f)(1)(i)(I)(*1*), and (f)(2)(i)(D) of the UK Substituted Compliance Notice and Proposed Order, *with* paras. (f)(1)(i)(G)(*1*), (f)(1)(i)(I)(*1*), and (f)(2)(i)(D) of the Order.

[469] *See* FCA Application at 127.

[470] *Compare* paras. (f)(1)(i)(G)(*1*), (f)(1)(i)(I)(*1*), and (f)(2)(i)(D) of the UK Substituted Compliance Notice and Proposed Order, *with* paras. (f)(1)(i)(G)(*1*), (f)(1)(i)(I)(*1*), and (f)(2)(i)(D) of the Order.

[471] *See* FCA Application at 203.

[472] *Compare* paras. (f)(1)(i)(K) and (f)(2)(i)(M) of the UK Substituted Compliance Notice and Proposed Order, *with* paras. (f)(1)(i)(K) and (f)(2)(i)(M) of the Order.

[473] *Compare* paras. (f)(1)(i)(A)(*1*), (f)(1)(i)(B)(*1*), (f)(1)(i)(C)(*1*), and (f)(1)(i)(F)(*1*) of the UK Substituted Compliance Notice and Proposed Order, *with* paras. (f)(1)(i)(A)(*1*), (f)(1)(i)(B)(*1*), (f)(1)(i)(C)(*1*), and (f)(1)(i)(F)(*1*) of the Order.

[474] *Compare* paras. (f)(2)(i)(A), (f)(2)(i)(B), (f)(2)(i)(D), and (f)(2)(i)(G)(*1*) of the UK Substituted Compliance Notice and Proposed Order, *with* paras. (f)(2)(i)(A), (f)(2)(i)(B), (f)(2)(i)(D), and (f)(2)(i)(G)(*1*) of the Order.

(with respect to PRA General Organisational Requirement 5.2),[475] both of which are relevant to employment application record creation but not employment application record preservation. Accordingly, the Commission is not removing references to these UK requirements from the Order's list of UK requirements comparable to Exchange Act rules 18a–5(a)(10) and (b)(8), but is removing references to these requirements from the Order's list of UK requirements comparable to Exchange Act rule 18a–6(d)(1).

The commenter recommended deleting from paragraphs (f)(1)(i)(K) and (f)(2)(i)(M) of the Order references to FCA SYSC 4.3A.1R and 4.3A.3R (management body), FCA SYSC 10.1.7R (managing conflicts), and FCA SYSC 27 (certification regime), reasoning that they do not correspond to, and go beyond, the requirements of Exchange Act rules 18a–5(a)(10) and (b)(8) (employment application record creation) and 18a–6(d)(1) (employment application record preservation). These provisions identify characteristics and standards applicable to a firm's employees, or require a conflicts of interest record to be maintained, which are relevant to employment application record creation but not employment application record preservation. Accordingly, the Commission is not removing references to these UK requirements from the Order's list of UK requirements comparable to Exchange Act rules 18a–5(a)(10) and (b)(8), but is removing references to these requirements from the Order's list of UK requirements comparable to Exchange Act rule 18a–6(d)(1).

The commenter recommended replacing in paragraph (f)(1)(i)(K) of the Order references to UK MiFID Org Reg article 21(1)(a) with references to UK MiFID Org Reg article 21(1)(d) due to an incorrect reference in the FCA Application with respect to Exchange Act rules 18a–5(a)(10) and (b)(8). The Commission agrees with the commenter's reasoning and is therefore replacing references to UK MiFID Org Reg article 21(1)(a) with references to UK MiFID Org Reg article 21(1)(d) in the Order's list of UK requirements comparable to Exchange Act rules 18a–5(a)(10) and (b)(8).[476]

The commenter recommended replacing in paragraphs (f)(1)(i)(N)(*1*) and (f)(1)(i)(O)(*1*) of the Order references to UK EMIR RTS article 15(1) with UK EMIR RTS article 15(1)(a) with respect to Exchange Act rules 18a–5(a)(18) and (b)(14) because the remainder of article 15(1) does not include a record creation requirement. The Commission agrees with the commenter's reasoning and is therefore replacing references to UK EMIR RTS article 15(1) with UK EMIR RTS article 15(1)(a) in the Order's list of UK requirements comparable to Exchange Act rules 18a–5(a)(18) and (b)(14).

The commenter recommended deleting from paragraph (f)(2)(E)(*1*) of the Order references to UK CRR and UK CRR Reporting ITS, which relate to supervisory reports to be made, reasoning that they do not correspond to, and go beyond, the requirements of Exchange Act rule 18a–6(b)(1)(v). Although these UK laws relate to reporting requirements, the information contained in these reports is relevant to the records required by Exchange Act rule 18a–6(b)(1)(v). In addition, the FCA Application specifically cites these requirements as comparable to Exchange Act rule 18a–6(b)(1)(v).[477] Accordingly, the Commission is not removing references to this UK requirement from the Order's list of UK requirements comparable to Exchange Act rule 18a–6(b)(1)(v).

The commenter recommended deleting from paragraph (f)(2)(i)(I)(*1*) of the Order references to UK CRR articles 286 and 293(1)(d), which relate to the use of internal models for credit risk, reasoning that they do not correspond to, and go beyond, the requirements of Exchange Act rule 18a–6(b)(1)(ix). The ''policies, processes and systems'' (with respect to UK CRR article 286) and ''adequate resources [ ] devoted to credit and counterparty risk control'' (with respect to UK CRR article 293(1)(d)) in practice require firms to maintain records relevant to Exchange Act rule 18a–6(b)(1)(ix). Accordingly, the Commission is not removing references to these UK requirements from the Order's list of UK requirements comparable to Exchange Act rule 18a–6(b)(1)(ix).

The commenter recommended deleting from paragraph (f)(2)(i)(I)(*1*) of the Order references to PRA Risk Control Rule 2.3, which sets a requirement that the management body approves and periodically reviews the strategies and policies for taking up, managing, monitoring, and mitigating risks, reasoning that it does not correspond to, and goes beyond, the requirements of Exchange Act rule 18a–6(b)(1)(ix). The Commission disagrees because in practice, this UK rule requires records to manage the firm's risks. Accordingly, the Commission is not removing references to this UK requirement from the Order's list of UK requirements comparable to Exchange Act rule 18a–6(b)(1)(ix).

The commenter recommended deleting from paragraph (f)(2)(i)(I)(*1*) of the Order references to UK EMIR RTS, reasoning that referencing an entire UK law without referencing a specific provision is does not correspond to, and goes beyond, the requirements of Exchange Act rule 18a–6(b)(1)(ix). This provision is cited by the FCA Application as directly relevant because it requires firms to ''implement formalised processes'' for ''identifying and resolving disputes,'' [478] which is relevant to Exchange Act rule 18a–6(b)(1)(ix). Accordingly, the Commission is not removing references to this UK requirement from the Order's list of UK requirements comparable to Exchange Act rule 18a–6(b)(1)(ix).

The commenter recommended deleting from paragraph (f)(2)(i)(M) of the Order references to FSMA sections 60A(2) and 63F(2), SMR Applications and Notifications Rules, PRA Certification Rules, PRA General Organisational Requirements Rules, and FCA SUP, reasoning that they do not correspond to, and go beyond, the requirements of Exchange Act rule 18a–6(d)(1). The Commission agrees with the commenter's reasoning because these provisions relate to record creation rather than record preservation, and is removing references to these UK requirements from the Order's list of UK requirements comparable to Exchange Act rule 18a–6(d)(1).

The commenter recommended deleting from paragraph (f)(2)(i)(O) of the Order references to FCA SYSC 6.1.1R and 10.1.6R, which relate to risk management control systems and risk control records, reasoning that they do not correspond to, and go beyond, the requirements of Exchange Act rule 18a–6(d)(3). However, the FCA Application cites these provisions as requiring ''the maintenance of a range of compliance policies and procedures'',[479] which is relevant to Exchange Act rule 18a–6(d)(3). Accordingly, the Commission is not removing references to these UK requirements from the Order's list of UK requirements comparable to Exchange Act rule 18a–6(d)(3).

The commenter recommended deleting from paragraph (f)(2)(i)(P)(*1*) of the Order references to FCA SYSC 4.1.1R(1), which is a general requirement concerning a firm's

[475] *See* FCA Application at 127.

[476] *Compare* para. (f)(1)(i)(K) of the UK Substituted Compliance Notice and Proposed Order, *with* para. (f)(1)(i)(K) of the Order.

[477] *See* FCA Application at 146–47.

[478] *See* FCA Application at 153–54.

[479] *See* FCA Application at 159–60.

governance, reasoning that it does not correspond to, and goes beyond, the requirements of Exchange Act rules 18a–6(d)(4) and (d)(5). However, the FCA Application cites this provision as requiring ''the maintenance of a range of risk management records'',[480] which is relevant to Exchange Act rules 18a–6(d)(4) and (d)(5). Accordingly, the Commission is not removing references to these UK requirements from the Order's list of UK requirements comparable to Exchange Act rules 18a–6(d)(4) and (d)(5).

The commenter recommended deleting from paragraph (f)(2)(i)(Q) of the Order references to FCA SYSC 4.1.1R(1), which is a general requirement concerning a firm's governance, reasoning that it does not correspond to, and goes beyond, the requirements of Exchange Act rule 18a–6(e). However, the FCA Application cites this provision as requiring ''sound security mechanisms in place to guarantee the security and authentication of the means of transfer of information, minimize the risk of data corruption and unauthorized access and to prevent information leakage maintaining the confidentiality of the data at all times'',[481] which is relevant to Exchange Act rule 18a–6(e). Accordingly, the Commission is not removing references to these UK requirements from the Order's list of UK requirements comparable to Exchange Act rule 18a–6(e).

c. Exchange Act Rule 18a–7

The commenter recommended deleting references to FSMA sections 137A, 137G, and 137T from paragraph (f)(3)(i)(A) reasoning that these provisions relate to the FCA's and PRA's powers to make rules and do not impose requirements on firms. Additionally, the commenter recommended deleting reference to CRD article 104(1)(j) reasoning that this provision does not form part of UK law. The Commission agrees with the commenter's reasoning and is removing references to these UK requirements from the list of UK requirements comparable to Exchange Act rules 18a–7(a)(1) and (a)(2).[482]

The commenter recommended deleting references to UK CRR rules that are set out in Part 8 of UK CRR relating to public disclosure in paragraph (f)(3)(ii)(A), reasoning that they do not correspond to, and go beyond, the requirements of Exchange Act rule 18a–7(a)(3) and Exchange Act rule 18a–7(j). However, the FCA application cites CRR articles 431, 433, 452, 454, and 455 as requiring, among other things, firms to make ''Pillar III' disclosures which include information on the use of capital models and matters such as credit risk, the exposure values by class of exposures subject to evaluation using models, and internal controls on the development and use of models.[483] This information is relevant to rule 18a–7(a)(3) and 18a–7(j). Accordingly, the Commission is removing references to UK CRR rules that are set out in Part 8 of UK CRR except for UK CRR articles 431, 433, 452, 454, and 455 in the Order's list of UK requirements comparable to Exchange Act rule 18a–7(a)(3) and 18a–7(j).[484]

The commenter recommended deleting references to FSMA sections 137A, 137G, and 137T in paragraph (f)(3)(ii)(A). As discussed above, the commenter has stated that these sections relate to the FCA's and the PRA's powers to make rules, and do not impose requirements on firms. The Commission agrees with this reasoning and is therefore removing references to these to these UK requirements from the Order's list of requirements comparable to Exchange Act rules 18a–7(a)(3) and 18a–7(j).[485]

The commenter recommended deleting from paragraph (f)(3)(iv)(A) references to the following FCA CASS sections: 6.2.2R, 6.6.2R, 6.6.3.R, 6.6.33G, 6.6.34R, 7.12.2R, 7.15.2R, 7.15.3R, 7.15.20R, and 7.15.21R. Additionally, the commenter recommended deleting references to FCA SUP sections 3.10.4R through 3.10.7R and the following UK CRR articles: 26(2), 132(5), 154, 191, 321, 325bi, 350, 353, 368, and 418. The commenter reasoned that these provisions do not correspond to, and go beyond, the requirements of Exchange Act rules 18a–7(c), (d), (e), (f), (g), and (h), and Exchange Act rule 18a–7(j). However, the FCA Application states that, pursuant to FCA CASS 6.2.2R, 6.62R, 6.63R, 6.6.33G, 6.6.34R 7.12.2R, 7.15.2R, 7.15.3R, 7.15.20R, and 7.15.21R, investment firms must ensure the segregation of client money and assets from those of the firm, maintain detailed records distinguishing client money and assets from those of the firm, and must conduct regular reconciliations between their accounts and records and those accounts and records of any third-parties with whom client money or assets may be held. Additionally, the FCA Application states that the that information about client money required under FCA CASS 7.12.2R, 7.15.2R, 7.15.3R, 7.15.20R, and 7.15.21R is comparable to the information required under Exchange Act rules 18a–7(c)(1)(i)(B) and 17a–7(c)(3) and (4).[486] Moreover, the FCA Application states that certain firms must have their financial statements audited pursuant to Companies Act section 475, and that under FCA SUP 3.8.5R and 3.10.4R through 3.10.7R an independent auditor must submit a client money and assets report to the FCA, within the prescribed time period and format, providing reasonable assurance that, among other things, the investment firm has maintained adequate systems to enable it to comply with the FCA CASS Rules. The FCA Application goes on to state that CRR article 26(2) relates to the inclusion of a firm's interim or year-end profits in Common Equity Tier 1 capital and the associated requirement that such profits be verified by persons independent of the firm, and that CRR articles 132(5) and 154 set forth requirements for a firm to engage an external auditor to confirm the accuracy of information regarding the firm's calculations with respect to average risk weights for certain exposures which is comparable to the requirements under Exchange Act rules 18a–7(c)(1)(i)(C) and 18a–7(d) through (g). Furthermore the FCA Application states that, for firms using internal models to calculate credit risk, operational risk, market risk exposures, or market risk capital requirement, CRR articles 191, 321, 325bi, and 368 require various levels of internal or external audit and/or review of the models, systems, and/or operations. The FCA application states where investment firms rely on a depository or management company of a collective investment undertaking, CRR articles 418, 350, and 353 require the investment firm to calculate and report own funds requirements for the market value of haircuts, and position risk with respect to positions in specified instruments.[487] As a result, the FCA Application states that the UK report review requirements provide for comparable regulatory outcomes to the SEC report review requirements, as both regulatory regimes require firms to submit reports by independent auditors on the firm's financial and operational information in order to ensure the accuracy of information and protect

[480] *See* FCA Application at 160–61.

[481] *See* FCA Application at 165.

[482] *Compare* para. (f)(3)(i)(A) of the UK Substituted Compliance Notice and Proposed Order, *with* para. (f)(3)(i)(A) of the Order.

[483] *See* FCA Application at 178–79.

[484] *Compare* para. (f)(3)(ii)(A) of the UK Substituted Compliance Notice and Proposed Order, *with* para. (f)(3)(ii)(A) of the Order.

[485] *Compare* para. (f)(3)(ii)(A) of the UK Substituted Compliance Notice and Proposed Order, *with* para. (f)(3)(ii)(A) of the Order.

[486] *See* FCA Application at 175–76.

[487] *See* FCA Application at 177 and 186–89.

market participants. The Commission believes these provisions are relevant to Exchange Act rules 18a–7(c), (d), (e), (f), (g), and (h). Accordingly, the Commission is not deleting references to these UK requirements from the Order's list of UK requirements comparable to Exchange Act rules 18a–7(c), (d), (e), (f), (g), and (h) and Exchange Act rule 18a–7(j).

The commenter recommended deleting from paragraph (f)(3)(iv)(A) reference to Capital Requirements 2013 Regulation 2(4), reasoning that this provision does not impose requirements directly on firms. The Commission agrees with the commenter's reasoning and, accordingly, is removing reference to this requirement from the Order's list of UK requirements comparable to Exchange Act rules 18a–7(c), (d), (e), (f), (g), and (h) and Exchange Act rule 18a–7(j). However, the FCA Application cites regulation 2(4) of the Capital Requirements (Country-by-Country Reporting) Regulations 2013 as relevant and which the Commission understands imposes reporting obligations directly on firms. As a result, the Commission is including reference to this requirement in the Order's list of UK requirements comparable to Exchange Act rule 18a–7(c), (d), (e), (f), (g), and (h) and Exchange Act rule 18a–7(j).[488]

d. Exchange Act Rule 18a–8

The commenter recommended deleting from paragraphs (f)(4)(i)(A)(*1*), (f)(4)(i)(B), (f)(4)(i)(C)(*1*), and (f)(4)(i)(D)(*1*) references to FCA SUP 15.3.12G and 15.3.14G, reasoning that these provisions are guidance. The Commission agrees. Accordingly, the removing reference to these requirements from the Order's list of UK requirements comparable to Exchange Act rule 18a–8(a)(1)((i), (a)(1)(ii), (b)(1), (b)(2), (b)(4), (c), (d), (e), and (h).[489]

The commenter recommended deleting from paragraphs (f)(4)(i)(A)(*1*), (f)(4)(i)(B), (f)(4)(i)(C)(*1*), and (f)(4)(i)(D)(*1*) references to: FCA SUP 15.3.15R, 15.3.17R, 15.3.21R; PRA Notifications Rules 2.6, 2.8, and 2.9; FCA CASS 6.657R, 7.15.33R, and Schedule 2; FCA SYSC 18.6.1R and 18.6.4G; and PRA General Organisational Requirements 2A.2, 2A.1(2), and 2A.3 to 2A.6. The commenter reasoned that these provisions do not correspond to, and go beyond, the requirements of Exchange Act rule 18a–8(a)(1)((i), (a)(1)(ii), (b)(1), (b)(2), (b)(4), (c), (d), (e), and (h). However, the FCA Application states that these provisions provide for a comparable regulatory outcome to the SEC notice requirements as these provisions require a CRR firm to notify the FCA immediately if the firm becomes aware of, or has information that reasonably suggests, that specified matters have occurred, may have occurred, or may occur in the foreseeable future. Additionally, specific notification obligations apply for breaches of requirements related to client money and assets, and with respect to civil, criminal, or disciplinary proceedings, fraud, errors, or other regularities, and insolvency, bankruptcy, and winding up. Furthermore, CRR firms must have procedures in place for employees to report a breach of, among other things, any rule, as well as appropriate arrangements for individuals, including employees, to disclose reportable concerns internally.[490] In practice, these provisions establish reporting mechanisms that will result in regulators being notified of events relevant to the disclosures required under rule 18a–8. Accordingly, the Commission is not deleting references to this UK requirement from the Order's list of UK requirements comparable to Exchange Act rule 18a–8(a)(1)((i), (a)(1)(ii), (b)(1), (b)(2), (b)(4), (c), (d), (e), and (h).

e. Exchange Act Rule 18a–9

The commenter recommends deleting from paragraph (f)(5)(*1*) references to FCA CASS 6.2.1R, 6.2.2R, 6.3.4A–1R, 6.3.6AR, 6.6.2R, 6.6.3R, 6.6.33G, 6.6.34R, 6.6.47G, 6.6.5G, 6.6.8R, 7.12.1R, 7.12.2R, 7.13.12R, 7.13.32R(3), 7.13.33R(3), 7.15.2R, 7.15.5R, 7.15.9R, 7.15.3R, 7.15.8R, 7.15.20R, 7.15.21G, 10.1.2G, 10.1.3R, 10.1.7, and 10.1.9E. The commenter also recommended deleting references to UK MiFID Org Reg articles 74 and 75, and to UK EMIR RTS article 12. The commenter reasoned that these provisions do not correspond to, and go beyond, the requirements of Exchange act rule 18a–9. With respect to FCA CASS 7.12R, 7.12.2R, 7.13.12R, 7.13.32R(3), 7.13.33R(3), 7.15.2R, 7.15.5R, 7.15.9R, 7.15.3R, 7.15.8R, 7.15.20R, and 7.15.21G the Commission agrees. These provisions relate to treatment of client money, and not the holding of client financial instruments. Accordingly, the Commission is removing references to these requirements from the Order's list of UK requirements comparable to Exchange Act rule 18a–9. Additionally, the Commission is removing references to FCA CASS 6.6.33G, 6.6.47G, and 6.6.5G as these provisions are non-binding guidance.[491]

With respect to the remaining provisions, the Commission disagrees. The FCA Applications states that, pursuant to FCA CASS 6.2.1R, firms holding financial instruments belonging to clients must make adequate arrangements to safeguard the ownership rights of clients and to prevent the use of a client's financial instruments on own account except with express consent of the client. To that end, the FCA Application states that the remaining provisions require investment firms to, among other things, maintain records enabling the firm to distinguish client assets from the firm's assets, including maintaining a client-specific safe custody asset record, and conduct on a regular basis reconciliations between internal accounts and records and those of any third-parties by whom client assets are held. Additionally, firms must ensure that client financial instruments deposited with third-party are identifiable separately from those of the firm and the third-party, and must minimize risk of loss of client assets. Moreover, the remaining provisions also require that checks and reconciliations must be carried out by a person who is independent of the production or maintenance of the records to be checked and/or reconciled, and must record any liens or rights of set-off against so that ownership is clear. Firms are also required, pursuant to the remaining provisions, to keep any internal records and accounts of client assets separate from any records the firm obtains from any third parties, and must also create specified records regarding each record check and reconciliation. Firms are required under the cited provision to keep detailed records in relation to every client order and decision to deal, and must also, with respect to verifying open transactions, comply with certain confirmation and portfolio reconciliation requirements for uncleared OTC derivatives contracts. Finally, firms must maintain a client asset resolution pack that can be used to achieve a timely return of client assets in a resolution scenario, as well as internal and external client asset reconciliations that must be available or retrievable within prescribed time

[488] *Compare* para. (f)(3)(iv)(A) of the UK Substituted Compliance Notice and Proposed Order, *with* para. (f)(3)(iv)(A) of the Order.

[489] *Compare* paras. (f)(4)(i)(A)(*1*), (f)(4)(i)(B), (f)(4)(i)(C)(*1*), and (f)(4)(i)(D)(*1*) of the UK Substituted Compliance Notice and Proposed Order, *with* paras. (f)(4)(i)(A)(*1*), (f)(4)(i)(B), (f)(4)(i)(C)(*1*), and (f)(4)(i)(D)(*1*) of the Order.

[490] *See* FCA Application at 181–85.

[491] *Compare* para. (f)(5)(*1*) of the UK Substituted Compliance Notice and Proposed Order, *with* para. (f)(5)(*1*) of the Order.

periods.[492] Based on these provisions, the FCA Application states that the UK periodic securities count requirements provide for a comparable regulatory outcome to the Commission's periodic securities count requirements.[493] The Commission believes these provisions are relevant to the requirements of rule 18a–9. Accordingly, the Commission is not removing references to these UK requirements from the Order's list of UK requirements comparable to Exchange Act rule 18a–9.

f. Exchange Act Section 15F(g)

The commenter recommended deleting from paragraph (f)(6) references to FCA COND at paragraphs 2C, 2D, 3B, 3C, 5D, and 5F, stating that these provisions set our certain minimum requirements for obtaining and maintaining PRA authorization. The commenter also recommended removing references in paragraph (f)(6) to PRA Fundamental Rules 2 and 6, and FCA PRIN 2.1.1R(2) and (3), stating that these provisions set out certain high-level principals for business. The commenter reasoned that these provisions do not correspond to, and go beyond, the requirements of Exchange Act section 15F(g). The Commission agrees with respect to references to FCA COND at paragraphs 2C, 2D, 3B, 3C, 5D, and 5F. Accordingly, the Commission is removing references to FCA COND at paragraphs 2C, 2D, 3B, 3C, 5D, and 5F from the Order's list of requirements comparable to Exchange Act section 15F(g).[494] However, the FCA Application states that pursuant to PRA Fundamental Rules 2 and 6, and FCA PRIN 2.1.1R(2) and (3) a UK firm must conduct its business with due skill, care, and diligence, and take reasonable care to organize and control its affairs responsibly and effectively. In practice, the FCA Application states that this will require UK firms to maintain adequate records and recordkeeping systems.[495] The Commission believes that these provisions are relevant to the requirements of Exchange Act section 15F(g). Accordingly, the Commission is not removing reference to these UK requirements from the Order's list of requirements comparable to Exchange Act section 15F(g).

IX. Supervisory and Enforcement Considerations

A. Preliminary Analysis

Exchange Act rule 3a71–6(a)(2)(i) provides that the Commission's assessments regarding the comparability of foreign requirements in part should take into account ''the effectiveness of the supervisory program administered, and the enforcement authority exercised'' by the foreign financial regulatory authority. This provision is intended to help ensure that substituted compliance is not predicated on rules that appear high-quality on paper if market participants in practice are allowed to fall short of their obligations, while also recognizing that differences among supervisory and enforcement regimes should not be assumed to reflect flaws in one regime or another.[496] The FCA Application accordingly included information regarding the supervisory and enforcement framework applicable to derivatives markets and market participants in the UK.

In proposing to grant substituted compliance in connection with the UK, the Commission preliminarily concluded that the relevant supervisory and enforcement considerations were consistent with substituted compliance. That preliminary conclusion took into account information regarding the FCA's and the PRA's roles and practices in supervising banks and investment firms located in the UK, as well as their enforcement-related authority and practices.[497]

B. Conclusions

Commenters did not address the Commission's preliminary conclusions regarding supervisory and enforcement considerations, and the Commission continues to conclude that the relevant supervisory and enforcement considerations in the UK are consistent with substituted compliance. In particular, based on the available information regarding the FCA's and the PRA's authority and practices to oversee market participants' compliance with applicable requirements and to take action in the event of violations, the Commission remains of the view that, consistent with rule 3a71–6, comparability determinations reflect UK requirements as they apply in practice.

To be clear, the supervisory and enforcement considerations addressed by rule 3a71–6 do not mandate that the Commission make judgments regarding the comparative merits of U.S. and foreign supervisory and enforcement frameworks, or to require specific findings regarding the supervisory and enforcement effectiveness of a foreign regime. The rule 3a71–6 considerations regarding supervisory and enforcement effectiveness instead address whether comparability analyses related to substituted compliance reflect requirements that market participants must follow, and for which market participants are subject to enforcement consequences in the event of violations. Those considerations are satisfied here.

X. Conclusion

It is hereby determined and ordered, pursuant to rule 3a71–6 under the Exchange Act, that a Covered Entity (as defined in paragraph (g)(1) of this Order) may satisfy the requirements under the Exchange Act that are addressed in paragraphs (b) through (f) of this Order so long as the Covered Entity is subject to and complies with relevant requirements of the United Kingdom and with the conditions of this Order, as amended or superseded from time to time.

(a) General Conditions.

This Order is subject to the following general conditions, in addition to the conditions specified in paragraphs (b) through (f):

(1) *Activities as UK ''regulated activities.''* For each condition in paragraphs (b) through (f) of this Order that requires the application of, and the Covered Entity's compliance with, provisions of FCA SYSC 4, 5, 6, 7, 9, and/or 10, PRA General Organisational Requirements, PRA Recordkeeping Rules, PRA Remuneration Rules, PRA Risk Control Rules, and/or MLR 2017, the Covered Entity's relevant security-based swap activities constitute ''regulated activities'' as defined for purposes of the relevant UK provisions, are carried on by the Covered Entity from an establishment in the United Kingdom, and fall within the scope of the Covered Entity's authorization from the FCA and/or the PRA to conduct regulated activities in the United Kingdom.

(2) *Activities as UK MiFID ''investment services or activities.''* For each condition in paragraphs (b) through (f) of this Order that requires the application of, and the Covered Entity's compliance with, provisions of FCA PROD 3 and/or UK MiFID Org Reg, the Covered Entity's relevant security-based swap activities (a) constitute ''investment services or activities,'' as defined in the FCA Handbook Glossary;

[492] *See* FCA Application at 129–36.

[493] *See* FCA Application at 129.

[494] *Compare* para. (f)(6) of the UK Substituted Compliance Notice and Proposed Order, *with* para. (f)(6) of the Order.

[495] *See* FCA Application at 102.

[496] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18404.

[497] *See* UK Substituted Compliance Notice and Proposed Order, 86 FR at 18404–06.

(b) are carried on by the Covered Entity from an establishment in the United Kingdom or from any other place that would cause FCA PROD 3 and/or UK MiFID Org Reg, as applicable, to apply to those activities, and (c) fall within the scope of the Covered Entity's authorization from the FCA and/or PRA to conduct regulated activities in the United Kingdom.

(3) *Activities as UK ''MiFID or equivalent third country business.''* For each condition in paragraphs (b) through (f) of this Order that requires the application of, and the Covered Entity's compliance with, provisions of FCA COBS 2, 4, 6, 8A, 9A, 14, and/or 16A, the Covered Entity's relevant security-based swap activities (a) constitute ''MiFID or equivalent third country business,'' as defined in the FCA Handbook Glossary; (b) are carried on by the Covered Entity from an establishment in the United Kingdom or from any other place that would cause FCA COBS 2, 4, 6, 8A, 9A, 14, and/or 16A, as applicable, to apply to those activities; and (c) fall within the scope of the Covered Entity's authorization from the FCA and/or PRA to conduct regulated activities in the United Kingdom.

(4) *Activities as UK ''designated investment business.''* For each condition in paragraphs (b) through (f) of this Order that requires the application of, and the Covered Entity's compliance with, provisions of FCA COBS 11, the Covered Entity's relevant security-based swap activities (a) constitute ''MiFID business'' that is also ''designated investment business,'' each as defined in the FCA Handbook Glossary; (b) are carried on by the Covered Entity from an establishment in the United Kingdom or from any other place that would cause FCA COBS 11, as applicable, to apply to those activities; and (c) fall within the scope of the Covered Entity's authorization from the FCA and/or PRA to conduct regulated activities in the United Kingdom.

(5) *Activities as UK ''MiFID business.''* For each condition in paragraphs (b) through (f) of this Order that requires the application of, and the Covered Entity's compliance with, provisions of FCA CASS 6 and/or 7, the Covered Entity is not an ICVC as defined in the FCA Handbook Glossary and the Covered Entity's relevant security-based swap activities constitute ''regulated activities'' as defined for purposes of the relevant UK provisions and ''MiFID business'' as defined in the FCA Handbook Glossary; are carried on by the Covered Entity from an establishment in the United Kingdom; and fall within the scope of the Covered Entity's authorization from the FCA and/or the PRA to conduct regulated activities in the United Kingdom.

(6) *Activities covered by FCA SYSC 10A.* For each condition in paragraphs (b) through (f) of this Order that requires the application of, and the Covered Entity's compliance with, provisions of FCA SYSC 10A, the Covered Entity's relevant security-based swap activities constitute activities described in FCA SYSC 10A.1.1(2)(a), (b), and/or (c); are carried on by the Covered Entity from an establishment in the United Kingdom and fall within the scope of the Covered Entity's authorization from the FCA and/or the PRA to conduct regulated activities in the United Kingdom.

(7) *Counterparties as UK MiFID ''clients.''* For each condition in paragraphs (b) through (f) of this Order that requires the application of, and the Covered Entity's compliance with, provisions of FCA CASS 6 and/or 7, FCA COBS 2, 4, 6, 8A, 9A, 11, 14, and/or 16A, FCA PROD 3, FCA SYSC 10.1.8, FCA SYSC 10A, and/or UK MiFID Org Reg, the relevant counterparty (or potential counterparty) to the Covered Entity is a ''client'' (or potential ''client''), as defined in COBS 3.2.1R.

(8) *Security-based swaps as UK MiFID ''financial instruments.''* For each condition in paragraphs (b) through (f) of this Order that requires the application of, and the Covered Entity's compliance with, provisions of FCA CASS 6 and/or 7, FCA COBS 2, 4, 6, 8A, 9A, 11, 14, and/or 16A, FCA PROD 3, FCA SYSC 10A, UK MAR, UK MAR Investment Recommendations Regulation, and/or UK MiFID Org Reg, the relevant security-based swap is a ''financial instrument,'' as defined in Part 1 of Schedule 2 of the UK Regulated Activities Order.

(9) *Covered Entity as UK CRD/CRR ''institution.''* For each condition in paragraph (b) through (f) of this Order that requires the application of, and the Covered Entity's compliance with, provisions of UK CRR, the Covered Entity is an ''institution,'' as defined in UK CRR article 4(1)(3).

(10) *Covered Entity as UK ''common platform firm'' or ''third country firm.''* For each condition in paragraph (b) through (f) of this Order that requires the application of, and the Covered Entity's compliance with, provisions of FCA SYSC 4, 5, 6, 7, 9, and/or 10, the Covered Entity is either a ''common platform firm'' (other than a ''UCITS investment firm'') or a ''third country firm,'' each as defined in the FCA Handbook Glossary.

(11) *Covered Entity as UK ''IFPRU investment firm.''* For each condition in paragraph (b) through (f) of this Order that requires the application of, and the Covered Entity's compliance with, provisions of FCA SYSC 19A, FCA IFPRU, and/or FCA BIPRU, the Covered Entity is an ''IFPRU investment firm,'' as defined in the FCA Handbook Glossary.

(12) *Covered Entity as ''UK bank'' or ''UK designated investment firm.''* For each condition in paragraph (b) through (f) of this Order that requires the application of, and the Covered Entity's compliance with, provisions of FCA SYSC 19D, PRA Internal Capital Adequacy Assessment Rules, PRA Internal Liquidity Adequacy Assessment Rules, PRA General Organisational Requirements, PRA Remuneration Rules, and/or PRA Risk Control Rules, the Covered Entity is a ''UK bank'' or ''UK designated investment firm,'' each as defined in the FCA Handbook Glossary (in the case of a provision of FCA SYSC 19D) or as defined in the PRA Rulebook Glossary (in the case of a provision of a PRA rule).

(13) *Covered Entity's counterparties as UK EMIR ''counterparties.''* For each condition in paragraphs (b) through (f) of this Order that requires the application of, and the Covered Entity's compliance with, provisions of UK EMIR, UK EMIR RTS, UK EMIR Margin RTS, and/or other UK requirements adopted pursuant to those provisions, if the relevant provision applies only to the Covered Entity's activities with specified types of counterparties, and if the counterparty to the Covered Entity is not any of the specified types of counterparty, the Covered Entity complies with the applicable condition of this Order:

(i) As if the counterparty were the specified type of counterparty; in this regard, if the Covered Entity reasonably determines that the counterparty would be a financial counterparty if it were established in the UK and authorized by an appropriate UK authority, it must treat the counterparty as if the counterparty were a financial counterparty; and

(ii) Without regard to the application of UK EMIR article 13.

(14) *Security-based swap status under UK EMIR.* For each condition in paragraphs (b) through (f) of this Order that requires the application of, and the Covered Entity's compliance with, provisions of UK EMIR, UK EMIR RTS, UK EMIR Margin RTS, and/or other UK requirements adopted pursuant to those provisions, if the relevant provision applies to the Covered Entity's OTC derivatives or OTC derivative contracts

that have not been cleared by a central counterparty, then either:

(i) The relevant security-based swap is an ''OTC derivative'' or ''OTC derivative contract,'' as defined in UK EMIR article 2(7), that has not been cleared by a central counterparty and otherwise is subject to the provisions of UK EMIR article 11, UK EMIR RTS articles 11 through 15, and UK EMIR Margin RTS article 2; or

(ii) The relevant security-based swap has been cleared by a central counterparty that is authorized, recognized, or taken to be recognized by a relevant UK authority to provide clearing services to clearing members or trading venues established in the UK.

(15) *Memorandum of Understanding with the FCA and the Bank of England (including in its capacity as the PRA).* The Commission has a supervisory and enforcement memorandum of understanding and/or other arrangement with the FCA and the Bank of England (including in its capacity as the PRA) addressing cooperation with respect to this Order at the time the Covered Entity complies with the relevant requirements under the Exchange Act via compliance with one or more provisions of this Order.

(16) *Notice to Commission.* A Covered Entity relying on this Order must provide notice of its intent to rely on this Order by notifying the Commission in writing. Such notice must be sent to the Commission in the manner specified on the Commission's website. The notice must include the contact information of an individual who can provide further information about the matter that is the subject of the notice. The notice must also identify each specific substituted compliance determination within paragraphs (b) through (f) of the Order for which the Covered Entity intends to apply substituted compliance. A Covered Entity must promptly provide an amended notice if it modifies its reliance on the substituted compliance determinations in this Order.

(17) *Notification Requirements Related to Changes in Capital.* A Covered Entity that is prudentially regulated relying on this Order must apply substituted compliance with respect to the requirements of Exchange Act rule 18a–8(c) and the requirements of Exchange Act rule 18a–8(h) as applied to Exchange Act rule 18a–8(c).

(b) Substituted Compliance in Connection With Risk Control Requirements

This Order extends to the following provisions related to risk control:

(1) *Internal risk management.* The requirements of Exchange Act section 15F(j)(2) and related aspects of Exchange Act rule 15Fh–3(h)(2)(iii)(I), provided that the Covered Entity is subject to and complies with the requirements of:

(i) FCA CASS 6.2.1R, 7.11.1R, and 7.12.1R;

(ii) FCA COBS 11.7A.3R;

(iii) Either {FCA IFPRU 2.2.7R(2), 2.2.17R through 2.2.28R, 2.2.30R, and 2.2.32R through 2.2.35R and FCA BIPRU 12.3.4R, 12.3.5R, 12.3.7R, 12.3.8R, 12.3.22AR, 12.3.22BR, 12.3.27R, 12.4.–2R, 12.4.–1R, 12.4.5AR, 12.4.10R, and 12.4.11R} or {PRA Internal Capital Adequacy Assessment Rules 4.1 through 4.4, 5.1, 6.1, 7.1, 7.2, 8.1 through 8.5, 9.1, 10.1, 10.2, and 11.1 through 11.3 and PRA Internal Liquidity Adequacy Assessment Rules 3.1, 3.2, 3.3, 4.1, 7.2, 8.1, 9.2, 11.1, 11.2, 11.4, 12.1, 12.3, and 12.4};

(iv) FCA PRIN 2.1.1R(3);

(v) FCA SYSC 4.1.1R(1), 4.1.2R, 4.3A.1R, 4.3A.2R, 4.3A.3R, 4.3A.4R, 7.1.4R, 7.1.17R, 7.1.18R, 7.1.18BR, 7.1.19R, 7.1.20R, 7.1.21R, 7.1.22R, 9.1.1AR, 10.1.3R, 10.1.7R, 10.1.8R, 10A.1.6R, 10A.1.8R, and 10A.1.11R and, if the Covered Entity is a UK bank or UK designated investment firm, also PRA General Organisational Requirements Rules 2.1, 2.2, and 5.1 through 5.3; PRA Record Keeping Rule 2.1; PRA Risk Control Rules 2.3, 2.7, and 3.1 through 3.5, and PRA Senior Management Functions Rule 8.2;

(vi) Either {FCA SYSC 19A.2.1R, 19A.3.1R(1), 19A.3.3R, 19A.3.7R through 19A.3.11R, 19A.3.13R, 19A.3.14R, 19A.3.16R, 19A.3.18R, 19A.3.22R, 19A.3.25R, 19A.3.27R, 19A.3.29R, 19A.3.30R, 19A.3.32R, 19A.3.35R, 19A.3.35AR, 19A.3.36R, 19A.3.38R, 19A.3.40R, 19A.3.40AR, 19A.3.44R through 19A.3.44DR, 19A.3.45R, 19A.3.47R, 19A.3.49R, 19A.3.51R, 19A.3.51AR, and 19A.3.52E} or {FCA SYSC 19D.2.1R, 19D.3.1R, 19D.3.3R, 19D.3.7R through 19D.3.12R, 19D.3.15R, 19D.3.17R, 19D.3.19R, 19D.3.23R, 19D.3.25R, 19D.3.27R, 19D.3.29R, 19D.3.31R, 19D.3.32R, 19D.3.34R, 19D.3.35R through 19D.3.39R, 19D.3.42R through 19D.3.45R, 19D.3.48R through 19D.3.52R, 19D.3.54R, 19D.3.56R, 19D.3.59R, 19D.3.61R, 19D.3.62R, 19D.3.63E, and 19D.3.64R and PRA Remuneration Rules 3.1, 4.2, 5.1, 5.3, 6.2, 6.3, 6.4, 7.2 through 7.4, 8.1, 8.2, 9.1, 11.1, 11.6, 12.1, 13.1, 14.1, and 15.2 through 15.23};

(vii) Either {FSMA schedule 6 part 2D and FCA COND 2.4.1A} or {FSMA schedule 6 parts 3C and 5D, FCA COND 2.4.1C, and PRA Fundamental Rules 3 through 6};

(viii) UK CRR articles 286 through 288 and 293;

(ix) UK EMIR Margin RTS article 2; and

(x) UK MiFID Org Reg articles 21 through 37 and 72 through 76 and Annex IV.

(2) *Trade acknowledgement and verification.* The requirements of Exchange Act rule 15Fi–2, provided that the Covered Entity is subject to and complies with the requirements of UK EMIR article 11(1)(a) and UK EMIR RTS article 12.

(3) *Portfolio reconciliation and dispute reporting.* The requirements of Exchange Act rule 15Fi–3, provided that:

(i) The Covered Entity is subject to and complies with the requirements of UK EMIR article 11(1)(b) and UK EMIR RTS articles 13 and 15; and

(ii) The Covered Entity provides the Commission with reports regarding disputes between counterparties on the same basis as it provides those reports to the FCA pursuant to UK EMIR RTS article 15(2).

(4) *Portfolio compression.* The requirements of Exchange Act rule 15Fi–4, provided that the Covered Entity is subject to and complies with the requirements of UK EMIR RTS article 14.

(5) *Trading relationship documentation.* The requirements of Exchange Act rule 15Fi–5, other than paragraph (b)(5) to that rule when the counterparty is a U.S. person, provided that the Covered Entity is subject to and complies with the requirements of UK EMIR article 11(1)(a), UK EMIR RTS article 12 and UK EMIR Margin RTS article 2.

(c) Substituted Compliance in Connection With Capital and Margin

(1) *Capital.* The requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1, and 18a–1a through d, provided that:

(i) The Covered Entity is subject to and complies with: UK CRR, Part One (General Provisions) Article 6(1), Part Two (Own Funds), Part Three (Capital Requirements), Part Four (Large Exposures), Part Five (Exposures to Transferred Credit Risk), Part Six (Liquidity), and Part Seven (Leverage); UK MiFID Org Reg article 23; UK EMIR Margin RTS, articles 2, 3(b), 7, and 19(1)(d) and (e), (3), and (8); PRA General Organisational Requirements Rule 2.1; PRA Fundamental Rules 2.4 and 2.5; PRA Risk Control Rules 2.3 and 3.1(1); PRA Capital Buffers Rules; PRA Internal Capital Adequacy Assessment

Rules; PRA Internal Liquidity Adequacy Assessment Rules; PRA Liquidity Coverage Requirement—UK Designated Investment Firms Rules; PRA Notifications Rules 2.1, 2.4 through 2.6, 2.8, 2.9; and Part 9 of the Bank Recovery and Resolution (No 2) Order 2014;

(ii) The Covered Entity applies substituted compliance for the requirements of Exchange Act rules 18a–5(a)(9), 18a–6(b)(1)(x), and 18a–8(a)(1)(i), (a)(1)(ii), (b)(1), (b)(2), and (b)(4) pursuant to this Order; and

(iii)(A) The Covered Entity:

(*1*) Maintains liquid assets as defined in paragraph (c)(1)(iii)(B) that have an aggregate market value that exceeds the amount of the Covered Entity's total liabilities by at least $100 million before applying the deduction specified in paragraph (c)(1)(iii)(C) and by at least $20 million after applying the deduction specified in paragraph (c)(1)(iii)(C);

(*2*) Makes and preserves for three years a quarterly record that:

(*a*) Identifies and values the liquid assets maintained pursuant to paragraph (c)(1)(iii)(A)(*1*);

(*b*) Compares the amount of the aggregate value the liquid assets maintained pursuant to paragraph (c)(1)(iii)(A)(*1*) to the amount of the Covered Entity's total liabilities and shows the amount of the difference between the two amounts (''the excess liquid assets amount''); and

(*c*) Shows the amount of the deduction specified in paragraph (c)(1)(iii)(C) and the amount that deduction reduces the excess liquid assets amount;

(*3*) The Covered Entity notifies the Commission in writing within 24 hours in the manner specified on the Commission's website if the Covered Entity fails to meet the requirements of paragraph (c)(iii)(A)(*1*) and includes in the notice the contact information of an individual who can provide further information about the failure to meet the requirements; and

(*4*) Includes its most recent statement of financial condition filed with its local supervisor (whether audited or unaudited) with its initial written notice to the Commission of its intent to rely on substituted compliance under condition (a)(16) above.

(B) For the purposes of paragraph (c)(1)(iii)(A)(*1*), liquid assets are:

(*1*) Cash and cash equivalents;

(*2*) Collateralized agreements;

(*3*) Customer and other trading related receivables;

(*4*) Trading and financial assets; and

(*5*) Initial margin posted by the Covered Entity to a counterparty or a third-party custodian, provided:

(*a*) The initial margin requirement is funded by a fully executed written loan agreement with an affiliate of the Covered Entity;

(*b*) The loan agreement provides that the lender waives re-payment of the loan until the initial margin is returned to the Covered Entity; and

(*c*) The liability of the Covered Entity to the lender can be fully satisfied by delivering the collateral serving as initial margin to the lender.

(C) The deduction required by paragraph (c)(1)(iii)(A) is the amount of the Covered Entity's risk-weighted assets calculated for the purposes of the capital requirements identified in paragraph (c)(1)(i) divided by 12.5.

(2) *Margin.* The requirements of Exchange Act section 15F(e) and Exchange Act rule 18a–3, provided that:

(i) The Covered Entity is subject to and complies with the requirements of UK EMIR article 11; UK EMIR Margin RTS; UK CRR articles 103, 105(3); 105(10); 111(2), 224, 285, 286, 286(7), 290, 295, 296(2)(b), 297(1), 297(3), and 298(1); UK MiFID Org Reg article 23(1); PRA General Organisational Requirements Rule 2.1; and PRA Internal Capital Adequacy Assessment Rule 4.2;

(ii) The Covered Entity collects variation margin, as defined in the UK EMIR Margin RTS, from a counterparty with respect to transactions in non-cleared security-based swaps, unless the counterparty would qualify for an exception from the collateral collection requirements under paragraph (c)(1)(iii) or (c)(2)(iii) of Exchange Act 18a–3;

(iii) The Covered Entity collects initial margin, as defined in the UK EMIR Margin RTS, from a counterparty with respect to transactions in non-cleared security-based swaps, unless the counterparty would qualify for an exception from the collateral collection requirements under paragraph (c)(1)(iii) of Exchange Act rule 18a–3; and

(iv) The Covered Entity applies substituted compliance for the requirements of Exchange Act rule 18a–5(a)(12) pursuant to this Order.

(d) Substituted Compliance in Connection With Internal Supervision and Compliance Requirements and Certain Exchange Act Section 15F(J) Requirements

This Order extends to the following provisions related to internal supervision and compliance and Exchange Act section 15F(j) requirements:

(1) *Internal supervision.* The requirements of Exchange Act rule 15Fh–3(h) and Exchange Act sections 15F(j)(4)(A) and (j)(5), provided that:

(i) The Covered Entity is subject to and complies with the requirements identified in paragraph (d)(3) of this Order;

(ii) The Covered Entity complies with paragraph (d)(4) of this Order; and

(iii) This paragraph (d) does not extend to the requirements of paragraph (h)(2)(iii)(I) to rule 15Fh–3 to the extent those requirements pertain to compliance with Exchange Act sections 15F(j)(2), (j)(3), (j)(4)(B), and (j)(6), or to the general and supporting provisions of paragraph (h) to rule 15Fh–3 in connection with those Exchange Act sections.

(2) *Chief compliance officers.* The requirements of Exchange Act section 15F(k) and Exchange Act rule 15Fk–1, provided that:

(i) The Covered Entity is subject to and complies with the requirements identified in paragraph (d)(3) of this Order;

(ii) All reports required pursuant to UK MiFID Org Reg article 22(2)(c) must also:

(A) Be provided to the Commission at least annually and in the English language;

(B) Include a certification signed by the chief compliance officer or senior officer (as defined in Exchange Act rule 15Fk–1(e)(2)) of the Covered Entity that, to the best of the certifier's knowledge and reasonable belief and under penalty of law, the report is accurate and complete in all material respects;

(C) Address the Covered Entity's compliance with:

(*1*) Applicable requirements under the Exchange Act; and

(*2*) The other applicable conditions of this Order in connection with requirements for which the Covered Entity is relying on this Order;

(D) Be provided to the Commission no later than 15 days following the earlier of:

(*1*) The submission of the report to the Covered Entity's management body; or

(*2*) The time the report is required to be submitted to the management body; and

(E) Together cover the entire period that the Covered Entity's annual compliance report referenced in Exchange Act section 15F(k)(3) and Exchange Act rule 15Fk–1(c) would be required to cover.

(3) *Applicable supervisory and compliance requirements.* Paragraphs (d)(1) and (d)(2) are conditioned on the Covered Entity being subject to and complying with the following requirements:

(i) FCA CASS 6.2.1R, 7.11.1R, and 7.12.1R;

(ii) FCA COBS 11.7A.3R;

(iii) Either {FCA IFPRU 2.2.7R(2), 2.2.17R through 2.2.28R, 2.2.30R, and

2.2.32R through 2.2.35R and FCA BIPRU 12.3.4R, 12.3.5R, 12.3.7R, 12.3.8R, 12.3.22AR, 12.3.22BR, 12.3.27R, 12.4.–2R, 12.4.–1R, 12.4.5AR, 12.4.10R, and 12.4.11R} or {PRA Internal Capital Adequacy Assessment Rules 4.1 through 4.4, 5.1, 6.1, 7.1, 7.2, 8.1 through 8.5, 9.1, 10.1, 10.2 and 11.1 through 11.3 and PRA Internal Liquidity Adequacy Assessment Rules 3.1, 3.2, 3.3, 4.1, 7.2, 8.1, 9.2, 11.1, 11.2, 11.4, 12.1, 12.3, and 12.4};

(iv) FCA PRIN 2.1.1R(3);

(v) FCA SYSC 4.1.1R(1), 4.1.2R, 4.3A.1R, 4.3A.2R, 4.3A.3R, 4.3A.4R, 7.1.4R, 7.1.17R, 7.1.18R, 7.1.18BR, 7.1.19R, 7.1.20R, 7.1.21R, 7.1.22R, 9.1.1AR, 10.1.3R, 10.1.7R, 10.1.8R, 10A.1.6R, 10A.1.8R, 10A.1.11R, and 24.2.6R(8) and, if the Covered Entity is a UK bank or UK designated investment firm, also PRA Allocation of Responsibilities Rule 4.1(16); PRA General Organisational Requirements Rules 2.1, 2.2, and 5.1 through 5.3; PRA Record Keeping Rule 2.1; PRA Risk Control Rules 2.3, 2.7, and 3.1 through 3.5; and PRA Senior Management Functions Rule 8.2;

(vi) Either {FCA SYSC 19A.2.1R, 19A.3.1R(1), 19A.3.3R, 19A.3.7R through 19A.3.11R, 19A.3.13R, 19A.3.14R, 19A.3.16R, 19A.3.18R, 19A.3.22R, 19A.3.25R, 19A.3.27R, 19A.3.29R, 19A.3.30R, 19A.3.32R, 19A.3.35R, 19A.3.35AR, 19A.3.36R, 19A.3.38R, 19A.3.40R, 19A.3.40AR, 19A.3.44R through 19A.3.44DR, 19A.3.45R, 19A.3.47R, 19A.3.49R, 19A.3.51R, 19A.3.51AR, and 19A.3.52E} or {FCA SYSC 19D.2.1R, 19D.3.1R, 19D.3.3R, 19D.3.7R through 19D.3.12R, 19D.3.15R, 19D.3.17R, 19D.3.19R, 19D.3.23R, 19D.3.25R, 19D.3.27R, 19D.3.29R, 19D.3.31R, 19D.3.32R, 19D.3.34R, 19D.3.35R through 19D.3.39R, 19D.3.42R through 19D.3.45R, 19D.3.48R through 19D.3.52R, 19D.3.54R, 19D.3.56R, 19D.3.59R, 19D.3.61R, 19D.3.62R, 19D.3.63E, and 19D.3.64R and PRA Remuneration Rules 3.1, 4.2, 5.1, 5.3, 6.2, 6.3, 6.4, 7.2, through 7.4, 8.1, 8.2, 9.1, 11.1, 11.6, 12.1, 13.1, 14.1, and 15.2 through 15.23};

(vii) Either {FSMA schedule 6 part 2D and FCA COND 2.4.1A} or {FSMA schedule 6 parts 3C and 5D, FCA COND 2.4.1C, and PRA Fundamental Rules 3 through 6};

(viii) UK CRR articles 286 through 288 and 293;

(ix) UK EMIR Margin RTS article 2; and

(x) UK MiFID Org Reg articles 21 through 37 and 72 through 76 and Annex IV.

(4) *Additional condition to paragraph (d)(1).* Paragraph (d)(1) further is conditioned on the requirement that the Covered Entity complies with the provisions specified in paragraph (d)(3) as if those provisions also require compliance with:

(i) Applicable requirements under the Exchange Act; and

(ii) The other applicable conditions of this Order in connection with requirements for which the Covered Entity is relying on this Order.

(e) Substituted Compliance in Connection With Counterparty Protection Requirements.

This Order extends to the following provisions related to counterparty protection:

(1) *Disclosure of information regarding material risks and characteristics.* The requirements of Exchange Act rule 15Fh–3(b) relating to disclosure of material risks and characteristics of one or more security-based swaps subject thereto, provided that the Covered Entity, in relation to that security-based swap, is subject to and complies with the requirements of:

(i) FCA COBS 2.2A.2R (excluding paragraph (1)(c) thereof), 6.1ZA.11R, 6.1ZA.12R, 6.2B.33R, 9A.3.6R, and 14.3A.3R; and

(ii) Either {UK MiFID Org Reg articles 48 through 50} or {FCA COBS 6.1ZA.9UK, 6.1ZA.14UK, and 14.3A.5UK}.

(2) *Disclosure of information regarding material incentives or conflicts of interest.* The requirements of Exchange Act rule 15Fh–3(b) relating to disclosure of material incentives or conflicts of interest that a Covered Entity may have in connection with one or more security-based swaps subject thereto, provided that the Covered Entity, in relation to that security-based swap, is subject to and complies with the requirements of either:

(i) FCA SYSC 10.1.8R and UK MiFID Org Reg articles 33 to 35;

(ii) FCA COBS 2.3A.5R, 2.3A.6R, 2.3A.7E, and 2.3A.10R through 2.3A.14R; or

(iii) UK MAR article 20(1) and UK MAR Investment Recommendations Regulation articles 5 and 6.

(3) ''*Know your counterparty.*'' The requirements of Exchange Act rule 15Fh–3(e), as applied to one or more security-based swap counterparties subject thereto, provided that the Covered Entity, in relation to the relevant security-based swap counterparty, is subject to and complies with the requirements of:

(i) FCA SYSC 6.1.1R;

(ii) UK MiFID Org Reg articles 21, 22, 25, and 26 and applicable parts of Annex I;

(iii) FCA SYSC 4.1.1R(1);

(iv) Either {FCA IFPRU 2.2.7R(2) and 2.2.32R} or {PRA General Organisational Requirement 2.1 and PRA Internal Capital Adequacy Assessment Rule 10.1};

(v) MLR 2017 Regulations 27 and 28; and

(vi) MLR 2017 Regulations 19(1) through (3), as applied to policies, controls, and procedures regarding customer due diligence.

(4) *Suitability.* The requirements of Exchange Act rule 15Fh–3(f), as applied to one or more recommendations of a security-based swap or trading strategy involving a security-based swap subject thereto, provided that:

(i) The Covered Entity, in relation to the relevant recommendation, is subject to and complies with the requirements of:

(A) FCA COBS 4.2.1R, 9A.2.1R, and 9A.2.16R;

(B) FCA PROD 3.2.1R and 3.3.1R;

(C) FCA SYSC 5.1.5AAR and 5.1.5ABR; and

(D) UK MiFID Org Reg articles 21(1)(b) and (d), 54, and 55; and

(ii) The counterparty to which the Covered Entity makes the recommendation is a ''professional client'' mentioned in FCA COBS 3.5.2R and is not a ''special entity'' as defined in Exchange Act section 15F(h)(2)(C) and Exchange Act rule 15Fh–2(d).

(5) *Fair and balanced communications.* The requirements of Exchange Act rule 15Fh–3(g), as applied to one or more communications subject thereto, provided that the Covered Entity, in relation to the relevant communication, is subject to and complies with the requirements of:

(i) Either {FCA COBS 2.1.1R and FCA COBS 4.2.1R} or {FCA COBS 2.1.1AR and FCA COBS 4.2.1R};

(ii) FCA COBS 2.2A.2R (excluding paragraph (1)(c) thereof), 2.2A.3R, 6.1ZA.11R, 6.1ZA.12R, 6.1ZA.13R, 6.2B.33R, 6.2B.34R, 9A.3.6R, and 14.3A.3R;

(iii) Either {UK MiFID Org Reg articles 46 through 48} or {FCA COBS 4.5A.9UK, 4.7.–1AUK, 6.1ZA.5UK, 6.1ZA.8UK, 6.1ZA.17UK, 6.1ZA.19UK, 6.1ZA.20UK, 8A.1.5UK to 8A.1.7UK, 14.3A.5UK, 14.3A.7UK, and 14.3A.9UK};

(iv) UK MAR Investment Recommendations Regulation articles 3 and 4; and

(v) UK MAR articles 12(1)(c), 15, and 20(1).

(6) *Daily mark disclosure.* The requirements of Exchange Act rule 15Fh–3(c), as applied to one or more security-based swaps subject thereto, provided that the Covered Entity is

required to reconcile, and does reconcile, the portfolio containing the relevant security-based swap on each business day pursuant to UK EMIR articles 11(1)(b) and 11(2) and UK EMIR RTS article 13.

(f) Substituted Compliance in Connection With Recordkeeping, Reporting, Notification, and Securities Count Requirements.

This Order extends to the following provisions that apply to a Covered Entity related to recordkeeping, reporting, notification, and securities counts:

(1)(i) *Make and keep current certain records.* The requirements of the following provisions of Exchange Act rule 18a–5, provided that the Covered Entity complies with the relevant conditions in this paragraph (f)(1)(i) and with the applicable conditions in paragraph (f)(1)(ii):

(A) The requirements of Exchange Act rule 18a–5(a)(1) or (b)(1), as applicable, provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of PRA Recordkeeping Rule 2.1; UK MiFID Org Reg articles 74, 75, and Annex IV; UK MiFIR article 25(1); and FCA SYSC 9.1.1AR; and

(*2*) With respect to the requirements of Exchange Act rule 18a–5(a)(1), the Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order.

(B) The requirements of Exchange Act rule 18a–5(a)(2), provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of PRA Recordkeeping Rule 2.1; FCA SYSC 9.1.1AR; PRA Internal Capital Adequacy Assessment Rule 3.1; FCA CASS 6, 7, 10.1.3R, 10.1.7, and 10.1.9E; UK MiFID Org Reg articles 72, 74, and 75; and UK EMIR article 39(4); and

(*2*) The Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order;

(C) The requirements of Exchange Act rule 18a–5(a)(3) or (b)(2), as applicable, provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of PRA Recordkeeping Rule 2.1; FCA SYSC 9.1.1AR; FCA CASS 6, 7, 10.1.3R, 10.1.7, and 10.1.9E; UK MiFID Org Reg articles 72, 74, and 75; and UK EMIR article 39(4); and

(*2*) With respect to the requirements of Exchange Act rule 18a–5(a)(3), the Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order;

(D) The requirements of Exchange Act rule 18a–5(a)(4) or (b)(3), as applicable, provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of UK CRR article 103; FCA COND at paragraphs 2C, 2D, 3B, 3C, 5D, and 5F; PRA Fundamental Rules 2 and 6; FCA PRIN 2.1.1.R(2) and (3); PRA Recordkeeping Rule 2.1; UK MiFID Org Reg articles 59, 74, 75 and Annex IV; UK MiFIR article 25(1); FCA SYSC 9.1.1AR; FCA COBS 16A.3.1UK; UK EMIR articles 9(2) and 11(1)(a); and

(*2*) With respect to the requirements of Exchange Act rule 18a–5(a)(4), the Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order;

(E) The requirements of Exchange Act rule 18a–5(b)(4) provided that the Covered Entity is subject to and complies with the requirements of FCA COBS 8A.1.9R, 16A.2.1R, 16A.3.1UK; UK MiFID Org Reg article 59; FCA SYSC 9.1.1AR; and UK EMIR articles 9(2) and 11(1)(a);

(F) The requirements of Exchange Act rule 18a–5(a)(5) or (b)(5), as applicable, provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of PRA Recordkeeping Rule 2.1; UK MiFID Org Reg articles 74, 75, and Annex IV; UK MiFIR article 25(1); and FCA SYSC 9.1.1AR; and

(*2*) With respect to the requirements of Exchange Act rule 18a–5(a)(5), the Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order;

(G) The requirements of Exchange Act rules 18a–5(a)(6) and (a)(15) or (b)(6) and (b)(11), as applicable, provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of PRA Fundamental Rules 2 and 6; PRA Recordkeeping Rule 2.1; CRR articles 103, 105(3), and 105(10); UK MiFID Org Reg articles 59, 74, 75, and Annex IV; UK MiFIR article 25(1); FCA SYSC 9.1.1AR; FCA COBS 8A.1.9R, 16A.2.1R, and 16A.3.1UK; UK EMIR articles 9(2), 11(1)(a), and 39(4); and

(*2*) The Covered Entity applies substituted compliance for the requirements of Exchange Act rule 15Fi–2 pursuant to this Order;

(H) The requirements of Exchange Act rule 18a–5(a)(7) or (b)(7), as applicable, provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of UK MiFIR article 25(1); MLR 2017 Regulations 28 through 30; FCA SYSC 9.1.1AR; and PRA Recordkeeping Rule 2.1; and

(*2*) With respect to the requirements of Exchange Act rule 18a–5(a)(7), the Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order;

(I) The requirements of Exchange Act rule 18a–5(a)(8), provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of CRR articles 103, 105(3), and 105(10); PRA Fundamental Rules 2 and 6; PRA Recordkeeping Rule 2.1; UK MiFID Org Reg articles 59, 74, 75, and Annex IV; UK MiFIR article 25(1); FCA SYSC 9.1.1AR; UK EMIR articles 9(2), 11(1)(a), and 39(4); MLR 2017 Regulations 28 through 30; and

(*2*) The Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order.;

(J) The requirements of Exchange Act rule 18a–5(a)(9), provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of PRA Internal Capital Adequacy Assessment Rule 3.1; FCA CASS 6, 7, 10.1.3R, 10.1.7, and 10.1.9E; UK EMIR article 39(4); and UK MiFID Org Reg articles 72, 74, and 75;

(*2*) The Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order; and

(*3*) This Order does not extend to the requirements of Exchange Act rule 18a–5(a)(9) relating to Exchange Act rule 18a–2;

(K) The requirements of Exchange Act rules 18a–5(a)(10) and (b)(8), provided that the Covered Entity is subject to and complies with the requirements of FSMA sections 63F(2), 63F(5), 63(2A), 60A(2); PRA Fitness and Propriety Rules 2.6 and 2.9; SMR Applications and Notifications Rules 2.1, 2.2, and 2.6; PRA Certification Rule 2.1; PRA General Organisational Requirements Rules 5.1 and 5.2; FCA SUP 10C.10.8D, 10C.10.8AD, 10C.15, 10C.10.16R, and 10C Annex 3D; FCA SYSC 4.3A.1R., 4.3A.3R, 10.1.7R, and 27; and UK MiFID Org Reg articles 21(1)(d) and 35;

(L) The requirements of Exchange Act rule 18a–5(a)(12), provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of UK CRR articles 103, 105(3), and

105(10); PRA Internal Capital Adequacy Assessment Rule 3.1; and MiFID Org Reg. articles 72, 74, and 75;

(*2*) The Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rule 18a–3 pursuant to this Order;

(M) The requirements of Exchange Act rules 18a–5(a)(17) and (b)(13), as applicable, regarding one or more provisions of Exchange Act rules 15Fh–3 or 15Fk–1 for which substituted compliance is available under this Order, provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of FCA COND at paragraphs 2C, 2D, 3B, 3C, 5D, and 5F; PRA Fundamental Rules 2 and 6; FCA PRIN 2.1.1.R(2) and (3); PRA Recordkeeping Rule 2.1; FCA SYSC 9.1.1AR; FCA COBS 9A.2.1R, UK MiFID Org Reg articles 72, 73, and Annex I; and UK EMIR article 39(5), in each case with respect to the relevant security-based swap or activity;

(*2*) With respect to the portion of Exchange Act rules 18a–5(a)(17) and (b)(13) that relates to one or more provisions of Exchange Act rule 15Fh–3 for which substituted compliance is available under this Order, the Covered Entity applies substituted compliance for such business conduct standard(s) of Exchange Act rule 15Fh–3 pursuant to this Order, as applicable, with respect to the relevant security-based swap or activity; and

(*3*) With respect to the portion of Exchange Act rules 18a–5(a)(17) and (b)(13) that relates to Exchange Act rule 15Fk–1, the Covered Entity applies substituted compliance for Exchange Act section 15F(k) and Exchange Act rule 15Fk–1 pursuant to this Order;

(N) The requirements of Exchange Act rules 18a–5(a)(18)(i) and (ii) or (b)(14)(i) and (ii), as applicable, provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of UK EMIR article 11(1)(b) and UK EMIR RTS article 15(1)(a); and

(*2*) The Covered Entity applies substituted compliance for Exchange Act rule 15Fi–3 pursuant to this Order; and

(O) The requirements of Exchange Act rule 18a–5(a)(18)(iii) or (b)(14)(iii), as applicable, provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of UK EMIR article 11(1)(b) and UK EMIR RTS article 15(1)(a), in each case with respect to such security-based swap portfolio(s); and

(*2*) The Covered Entity applies substituted compliance for Exchange Act rule 15Fi–4 pursuant to this Order.

(ii) Paragraph (f)(1)(i) is subject to the following further conditions:

(A) Paragraphs (f)(1)(i)(A) through (D) and (H) are subject to the condition that the Covered Entity preserves all of the data elements necessary to create the records required by the applicable Exchange Act rules cited in such paragraphs and upon request furnishes promptly to representatives of the Commission the records required by those rules;

(B) A Covered Entity may apply the substituted compliance determination in paragraph (f)(1)(i)(M) to records of compliance with Exchange Act rule 15Fh–3(b), (c), (e), (f), and (g) in respect of one or more security-based swaps or activities related to security-based swaps; and

(C) This Order does not extend to the requirements of Exchange Act rule 18a–5(a)(13), (a)(14), (a)(16), (b)(9), (b)(10), or (b)(12).

(2)(i) *Preserve certain records.* The requirements of the following provisions of Exchange Act rule 18a–6, provided that the Covered Entity complies with the relevant conditions in this paragraph (f)(2)(i) and with the applicable conditions in paragraph (f)(2)(ii):

(A) The requirements of Exchange Act rule 18a–6(a)(1) or (a)(2), as applicable, provided that the Covered Entity is subject to and complies with the requirements of UK MiFID Org Reg articles 72, 74, 75, and Annex IV; FCA SYSC 9.1.1AR and 9.1.2R; FSMA section 165; PRA Internal Capital Adequacy Assessment Rule 3.1; PRA Fundamental Rules 2 and 6; PRA Recordkeeping Rules 2.1 and 2.2; FCA PRIN 2.1.1.R(2) and (3); FCA CASS 6, 7, 10.1.3R, 10.1.7, and 10.1.9E; UK CRR article 103; FCA COND at paragraphs 2C, 2D, 3B, 3C, 5D, and 5F; UK MiFIR article 25(1); and UK EMIR article 9(2);

(B) The requirements of Exchange Act rule 18a–6(b)(1)(i) or (b)(2)(i), as applicable, provided that the Covered Entity is subject to and complies with the requirements of UK MiFID Org Reg articles 72, 74, 75, and Annex IV; FCA SYSC 9.1.1AR and 9.1.2R; FSMA section 165; PRA Internal Capital Adequacy Assessment Rule 3.1; PRA Fundamental Rules 2 and 6; PRA Recordkeeping Rules 2.1 and 2.2; FCA PRIN 2.1.1.R(2) and (3); FCA CASS 6, 7, 10.1.3R, 10.1.7, and 10.1.9E; UK CRR article 103; FCA COND at paragraphs 2C, 2D, 3B, 3C, 5D, and 5F; UK MiFIR article 25(1); and UK EMIR article 9(2);

(C) The requirements of Exchange Act rules 18a–6(b)(1)(ii) and (iii), provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of PRA Internal Capital Adequacy Assessment Rule 3.1; FCA CASS 6, 7, 10.1.3R, 10.1.7, and 10.1.9E; UK MiFID Org Reg articles 72, 74, and 75; PRA Recordkeeping Rules 2.1 and 2.2; FCA SYSC 9.1.1AR and 9.1.2R; and UK EMIR article 9(2); and

(*2*) The Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order;

(D) The requirements of Exchange Act rule 18a–6(b)(1)(iv) or (b)(2)(ii), as applicable, provided that the Covered Entity is subject to and complies with the requirements of PRA Fundamental Rules 2 and 6; PRA Recordkeeping Rules 2.1 and 2.2; UK CRR article 103; FCA SYSC 9.1.1AR, 9.1.2R, 10A.1.6R, and 10A.1.8R; UK MiFID Org Reg articles 72, 73, 74, 75, 76, Annex I, and Annex IV; UK MiFIR article 25(1); and UK EMIR article 9(2);

(E) The requirements of Exchange Act rule 18a–6(b)(1)(v), provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of UK EMIR article 9(2); UK CRR articles 99, 294, 394, 415, 430, and Part Six: Title II and Title III; UK CRR Reporting ITS article 14 and annexes I–V and VIII–XIII; PRA Recordkeeping Rules 2.1 and 2.2; FCA SYSC 9.1.1AR and 9.1.2R; and UK MiFID Org Reg article 72(1);

(*2*) With respect to the requirements of Exchange Act rule 18a–6(b)(1)(v), the Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant this Order; and

(*3*) This Order does not extend to the requirements of Exchange Act rule 18a–6(b)(1)(v) relating to Exchange Act rule 18a–2;

(F) The requirements of Exchange Act rule 18a–6(b)(1)(vi) or (b)(2)(iii), as applicable, provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of PRA Recordkeeping Rules 2.1 and 2.2; FCA SYSC 9.1.1AR and 9.1.2R; UK MiFID Org Reg articles 72(1) and 73; and UK EMIR article 9(2); and

(*2*) With respect to the requirements of Exchange Act rule 18a–6(b)(1)(vi), the Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order;

(G) The requirements of Exchange Act rule 18a–6(b)(1)(vii) or (b)(2)(iv), as applicable, provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of PRA Recordkeeping Rules 2.1 and 2.2; FCA SYSC 9.1.1AR and 9.1.2R; UK

MiFID Org Reg articles 72(1) and 73; UK MiFIR article 25(1); and UK EMIR article 9(2); and

(*2*) With respect to the requirements of Exchange Act rule 18a–6(b)(1)(vii), the Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order;

(H) The requirements of Exchange Act rule 18a–6(b)(1)(viii), provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of UK CRR articles 99, 294, 394, 415, 430, and Part Six: Title II and Title III; UK CRR Reporting ITS article 14 and annexes I–V and VIII–XIII, as applicable; PRA Recordkeeping Rules 2.1 and 2.2; FCA SYSC 9.1.1AR and 9.1.2R; and UK MiFID Org Reg article 72(1);

(*2*) The Covered Entity applies substituted compliance for the requirements of Exchange Act rule 18a–7(a)(1), (b), (c) through (h), and Exchange Act rule 18a–7(j) as applied to these requirements pursuant to this Order;

(*3*) With respect to the requirements of Exchange Act rule 18a–6(b)(1)(viii), the Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order;

(*4*) This Order does not extend to the requirements of Exchange Act rule 18a–6(b)(1)(viii)(L); and

(*5*) This Order does not extend to the requirements of Exchange Act rule 18a–6(b)(1)(viii)(M) relating to Exchange Act rule 18a–2.

(I) The requirements of Exchange Act rule 18a–6(b)(1)(ix), provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of FCA SYSC 4.1.1R(1), 6.1.1R, 7.1.4R, 9.1.1AR, 9.1.2R, and 10.1.7R; FCA COBS 2.3A.32R; UK MiFID Org Reg articles 22(3)(c), 23, 24, 25(2), 26, 29(2)(c), 35, and 72(1); PRA Risk Control Rule 2.3; PRA Internal Capital Adequacy Assessment Rules 3 through 11; UK CRR articles 176, 286, and 293(1)(d); UK EMIR RTS; PRA Recordkeeping Rule 2.1 and 2.2; and UK EMIR article 9(2); and

(*2*) The Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order;

(J) The requirements of Exchange Act rule 18a–6(b)(1)(x), provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of PRA Internal Capital Adequacy Assessment Rules 3.1 and 13.2; PRA Recordkeeping Rules 2.1 and 2.2; FCA SYSC 9.1.1AR and 9.1.2R; UK MiFID Org Reg article 72(1); and UK EMIR article 9(2); and

(*2*) The Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order;

(K) The requirements of Exchange Act rule 18a–6(b)(1)(xii) or (b)(2)(vii), as applicable, regarding one or more provisions of Exchange Act rules 15Fh–3 or 15Fk–1 for which substituted compliance is available under this Order, provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of MLR 2017 Regulations 27 through 30; PRA Recordkeeping Rule 2.1 and 2.2; FCA SYSC 9.1.1AR and 9.1.2R; UK MiFID Org Reg article 72(1); and UK EMIR article 9(2), in each case with respect to the relevant security-based swap or activity;

(*2*) With respect to the portion of Exchange Act rule 18a–6(b)(1)(xii) or (b)(2)(vii) that relates to one or more provisions of Exchange Act rule 15Fh–3 for which substituted compliance is available under this Order, the Covered Entity applies substituted compliance for such business conduct standard(s) of Exchange Act rule 15Fh–3 pursuant to this Order, as applicable, with respect to the relevant security-based swap or activity; and

(*3*) With respect to the portion of Exchange Act rule 18a–6(b)(1)(xii) or (b)(2)(vii), as applicable, that relates to Exchange Act rule 15Fk–1, the Covered Entity applies substituted compliance for Exchange Act section 15F(k) and Exchange Act rule 15Fk–1 pursuant to this Order;

(L) The requirements of Exchange Act rule 18a–6(c), provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of PRA Recordkeeping Rules 2.1 and 2.2; FCA SYSC 9.1.1AR and 9.1.2R; and UK MiFID Org Reg articles 21(1)(f) and 72(1); and

(*2*) This Order does not extend to the requirements of Exchange act rule 18a–6(c) relating to Forms SBSE, SBSE–A, SBSE–C, SBSE–W, all amendments to these forms, and all other licenses or other documentation showing the registration of the Covered Entity with any securities regulatory authority or the U.S. Commodity Futures Trading Commission;

(M) The requirements of Exchange Act rule 18a–6(d)(1), provided that the Covered Entity is subject to and complies with the requirements of FSMA sections 63(2A) and 63F(5); FCA SYSC 9.1.1AR and 9.1.2R; UK MiFID Org Reg articles 35 and 72(1); and PRA Recordkeeping Rules 2.1 and 2.2;

(N) The requirements of Exchange Act rule 18a–6(d)(2), provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of PRA Recordkeeping Rules 2.1 and 2.2; FCA SYSC 9.1.1AR and 9.1.2R; UK MiFID Org Reg articles 72(1) and 72(3); and UK EMIR article 9(2); and

(*2*) With respect to the requirements of Exchange Act rule 18a–6(d)(2)(i), the Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order;

(O) The requirements of Exchange Act rule 18a–6(d)(3), provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of FCA COND at paragraphs 2C, 2D, 3B, 3C, 5D, and 5F; PRA Fundamental Rules 2 and 6; FCA PRIN 2.1.1.R(2) and (3); FCA SYSC 6.1.1R, 9.1.1AR, 9.1.2R, 10A.1.6R; PRA Recordkeeping Rules 2.1 and 2.2; UK MiFID Org Reg articles 21(1)(f), 72, and Annex I; and

(*2*) With respect to the requirements of Exchange Act rule 18a–6(d)(3)(i), the Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order;

(P) The requirements of Exchange Act rules 18a–6(d)(4) and (d)(5), provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of FCA COBS 8A.1.9R; PRA Recordkeeping Rules 2.1 and 2.2; FCA SYSC 4.1.1R(1), 6.1.1, 9.1.1AR, and 9.1.2R; UK MiFID Org Reg articles 24, 25(2), 72(1), and 73; and UK EMIR article 9(2); and

(*2*) The Covered Entity applies substituted compliance for Exchange Act rules 15Fi–3, 15Fi–4, and 15Fi–5 pursuant to this Order;

(Q) The requirements of Exchange Act rule 18a–6(e), provided that the Covered Entity is subject to and complies with the requirements of PRA Recordkeeping Rule 2.1; FCA SYSC 4.1.1R, 9.1.1AR, and 9.1.2R; and UK MiFID Org Reg articles 21(2), 58, 72(1), and 72(3); and

(R) The requirements of Exchange Act rule 18a–6(f), provided that the Covered Entity is subject to and complies with the requirements of PRA Outsourcing Rule 2.1; FCA SYSC 8.1.1R; and UK MiFID Org Reg articles 31(1).

(ii) Paragraph (f)(2)(i) is subject to the following further conditions:

(A) A Covered Entity may apply the substituted compliance determination in paragraph (f)(2)(i)(K) to records related to Exchange Act rule 15Fh–3(b),

(c), (e), (f), and (g) in respect of one or more security-based swaps or activities related to security-based swaps; and

(B) This Order does not extend to the requirements of Exchange Act rule 18a–6(b)(1)(xi), (b)(1)(xiii), (b)(2)(v), (b)(2)(vi), or (b)(2)(viii).

(3) *File Reports.* The requirements of the following provisions of Exchange Act rule 18a–7, provided that the Covered Entity complies with the relevant conditions in this paragraph (f)(3):

(i) The requirements of Exchange Act rule 18a–7(a)(1) or (a)(2), as applicable, and the requirements of Exchange Act rule 18a–7(j) as applied to the requirements of Exchange Act rule 18a–7(a)(1) or (a)(2), as applicable, provided that:

(A) The Covered Entity is subject to and complies with the requirements of PRA Definition of Capital Rule 4.5; UK CRR articles 99, 394, 430, and Part Six: Title II and Title III; and UK CRR Reporting ITS annexes I, II, III, IV, V, VIII, IX, X, XI, XII, and XIII, as applicable;

(B) The Covered Entity files periodic unaudited financial and operational information with the Commission or its designee in the manner and format required by Commission rule or order and presents the financial information in the filing in accordance with generally accepted accounting principles that the Covered Entity uses to prepare general purpose publicly available or available to be issued financial statements in the UK.;

(C) With respect to the requirements of Exchange Act rule 18a–7(a)(1), the Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order; and

(D) With respect to the requirements of Exchange Act rule 18a–7(a)(1), the Covered Entity applies substituted compliance for the requirements of Exchange Act rule 18a–6(b)(1)(viii) pursuant to this Order;

(ii) The requirements of Exchange Act rule 18a–7(a)(3) and the requirements of Exchange Act rule 18a–7(j) as applied to the requirements of paragraph (a)(3) of Exchange Act rule 18a–7, provided that:

(A) The Covered Entity is subject to and complies with the requirements of UK CRR articles 99, 394, 431, 433, 452, 454, and 455; UK CRR Reporting ITS annexes I, II, VIII, and IX, as applicable; PRA Definition of Capital Rule 4.5; and Companies Act sections 394, 415, 442, and 475; and

(B) The Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order;

(iii) The requirements of Exchange Act rule 18a–7(b), provided that:

(A) the Covered Entity is subject to and complies with the requirements of UK CRR articles 431 through 455; and Companies Act sections 394, 415, 442, and 475; and

(B) the Covered Entity applies substituted compliance for the requirements of Exchange Act rule 18a–6(b)(1)(viii) pursuant to this Order;

(iv) The requirements of Exchange Act rule 18a–7(c), (d), (e), (f), (g), and (h) and the requirements of Exchange Act rule 18a–7(j) as applied to the requirements of paragraphs (c), (d), (e), (f), (g), and (h) of Exchange Act rule 18a–7, provided that:

(A) The Covered Entity is subject to and complies with the requirements of FCA CASS 6.2.2R, 6.6.2R, 6.6.3R, 6.6.33G, 6.6.34R, 7.12.2R, 7.15.2R, 7.15.3R, 7.15.20R, and 7.15.21R; FCA SUP 3.8.5R, 3.10.4R through 3.10.7R; UK CRR articles 26(2), 132(5), 154, 191, 321, 325bi, 350, 353, 368, 418; Companies Act section 475; and the Capital Requirements (Country-by-Country Reporting) Regulations 2013 Regulation 2(4);

(B) With respect to financial statements the Covered Entity is required to file annually with the UK PRA or FCA, including a report of an independent public accountant covering the financial statements, the Covered Entity:

(*1*) Simultaneously sends a copy of such annual financial statements and the report of the independent public accountant covering the annual financial statements to the Commission in the manner specified on the Commission's website;

(*2*) Includes with the transmission the contact information of an individual who can provide further information about the financial statements and report;

(*3*) Includes with the transmission the report of an independent public accountant required by Exchange Act rule 18a–7(c)(1)(i)(C) covering the annual financial statements if UK laws do not require the Covered Entity to engage an independent public accountant to prepare a report covering the annual financial statements; provided, however, that such report of the independent public accountant may be prepared in accordance with generally accepted auditing standards in UK that the independent public accountant uses to perform audit and attestation services and the accountant complies with UK independence requirements;

(*4*) Includes with the transmission the reports required by Exchange Act rules 18a–7(c)(1)(i)(B) and (C) addressing the statements identified in Exchange Act rule 18a–7(c)(3) or (c)(4), as applicable, that relate to Exchange Act rule 18a–4; provided, however, that the report of the independent public accountant required by Exchange Act rule 18a–7(c)(1)(i)(C) may be prepared in accordance with generally accepted auditing standards in the UK that the independent public accountant uses to perform audit and attestation services and the accountant complies with UK independence requirements;

(*5*) Includes with the transmission the supporting schedules and reconciliations, as applicable, required by Exchange Act rules 18a–7(c)(2)(ii) and (iii), respectively, relating to Exchange Act rule 18a–2; and

(*6*) Includes with the transmission the supporting schedules and reconciliations, as applicable, required by Exchange Act rules 18a–7(c)(2)(ii) and (iii), respectively, relating to Exchange Act rules 18a–4 and 18a–4a;

(C) The Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order; and

(D) The Covered Entity applies substituted compliance for the requirements of Exchange Act rule 18a–6(b)(1)(viii) pursuant to this Order.

(v) The requirements of Exchange Act rule 18a–7(i), provided that:

(A) The Covered Entity is subject to and complies with the requirements of FCA SUP 16.3.17R and PRA Regulatory Reporting Rule 18; and

(B) The Covered Entity:

(*1*) Simultaneously sends a copy of any notice required to be sent by UK law cited in paragraph (f)(3)(v)(A) of the Order to the Commission in the manner specified on the Commission's website; and

(*2*) Includes with the transmission the contact information of an individual who can provide further information about the matter that is the subject of the notice.

(4)(i) *Provide Notification.* The requirements of the following provisions of Exchange Act rule 18a–8, provided that the Covered Entity complies with the relevant conditions in this paragraph (f)(4)(i) and with the applicable conditions in paragraph (f)(4)(ii):

(A) The requirements of paragraphs (a)(1)(i), (a)(1)(ii), (b)(1), (b)(2), and (b)(4) of Exchange Act rule 18a–8 and the requirements of Exchange Act rule 18a–8(h) as applied to the requirements of

paragraphs (a)(1)(i), (a)(1)(ii), (b)(1), (b)(2), and (b)(4) of Exchange Act rule 18a–8, provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of FCA PRIN 2.1.1R (Principle 11); PRA Fundamental Rule 7; FCA SUP 15.3.1R, 15.3.11R, 15.3.15R, 15.3.17R, and 15.3.21R; PRA Notifications Rules 2.1, 2.4, 2.5, 2.6, 2.8, and 2.9; FCA SYSC 18.6.1R; PRA General Organisational Requirements 2A.2, 2A.1(2) and 2A.3 to 2A.6; and CRR article 366(5); and

(*2*) The Covered Entity applies substituted compliance with respect to the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order;

(B) The requirements of Exchange Act rule 18a–8(c) and the requirements of Exchange Act rule 18a–8(h) as applied to Exchange Act rule 18a–8(c), provided that the Covered Entity is subject to and complies with the requirements of FCA PRIN 2.1.1R (Principle 11); PRA Fundamental Rule 7; FCA SUP 15.3.1R, 15.3.11R, 15.3.15R, 15.3.17R, and 15.3.21R; FCA CASS 6.6.57R and 7.15.33R; PRA Notifications Rules 2.1, 2.4, 2.5, 2.6, 2.8, and 2.9; FCA SYSC 18.6.1R; and PRA General Organisational Requirements 2A.2, 2A.1(2), and 2A.3 to 2A.6;

(C) The requirements of Exchange Act rule 18a–8(d) and the requirements of Exchange Act rule 18a–8(h) as applied to the requirements of Exchange Act rule 18a–8(d), provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of FCA PRIN 2.1.1R (Principle 11); PRA Fundamental Rule 7; FCA SUP 15.3.1R, 15.3.11R, 15.3.15R, 15.3.17R, and 15.3.21R; FCA CASS 6.6.57R and 7.15.33R; PRA Notifications Rules 2.1, 2.4, 2.5, 2.6, 2.8, and 2.9; FCA SYSC 18.6.1R; and PRA General Organisational Requirements 2A.2, 2A.1(2), and 2A.3 through 2A.6; and

(*2*) This Order does not extend to the requirements of Exchange Act rule 18a–8(d) to give notice with respect to books and records required by Exchange Act rule 18a–5 for which the Covered Entity does not apply substituted compliance pursuant to this Order;

(D) The requirements of Exchange Act rule 18a–8(e) and the requirements of Exchange Act rule 18a–8(h) as applied to the requirements of Exchange Act rule 18a–8(e), provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of FCA PRIN 2.1.1R (Principle 11); PRA Fundamental Rule 7; FCA SUP 15.3.1R, 15.3.11R, 15.3.15R, 15.3.17R, and 15.3.21R; FCA CASS 6.6.57R and 7.15.33R; PRA Notifications Rules 2.1, 2.4, 2.5, 2.6, 2.8, and 2.9; FCA SYSC 18.6.1R; and PRA General Organisational Requirements 2A.2, 2A.1(2), and 2A.3 through 2A.6;

(*2*) The Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order;

(*3*) This Order does not extend to the requirements of Exchange act rule 18a–8(e) relating to Exchange Act rule 18a–2 or to the requirements of Exchange Act rule 18a–8(h) as applied to the requirements Exchange Act rule 18a–8(e) relating to Exchange Act rule 18a–2; and

(*4*) This Order does not extend to the requirements of Exchange act rule 18a–8(e) relating to Exchange Act rule 18a–4 or to the requirements of Exchange Act rule 18a–8(h) as applied to the requirements of Exchange Act rule 18a–8(e) relating to Exchange Act rule 18a–4;

(ii) Paragraph (f)(4)(i) is subject to the following further conditions:

(A) The Covered Entity:

(*1*) Simultaneously sends a copy of any notice required to be sent by UK law cited in this paragraph of the Order to the Commission in the manner specified on the Commission's website; and

(*2*) Includes with the transmission the contact information of an individual who can provide further information about the matter that is the subject of the notice.

(B) This Order does not extend to the requirements of paragraphs (a)(2) and (b)(3) of Exchange Act rule 18a–8 relating to Exchange Act rule 18a–2 or to the requirements of Exchange Act rule 18a–8(h) as applied to the requirements of paragraphs (a)(2) and (b)(3) of Exchange Act rule 18a–8 relating to Exchange Act rule 18a–2; and

(C) This Order does not extend to the requirements of paragraph (g) of Exchange Act rule 18a–8 or to the requirements of Exchange Act rule 18a–8(h) as applied to the requirements of paragraph (g) of Exchange Act rule 18a–8.

(5) *Securities Counts.* The requirements of Exchange Act rule 18a–9, provided that:

(*1*) The Covered Entity is subject to and complies with the requirements of FCA CASS 6.2.1R, 6.2.2R, 6.3.4A–1R, 6.3.6AR, 6.6.2R, 6.6.3R, 6.6.34R, 6.6.4R, 6.6.8R, 10.1.3R, 10.1.7R, and 10.1.9E; FCA SUP 3.10.4R through 3.10.7R; UK MiFID Org Reg articles 74 and 75; UK EMIR article 11(1)(b); and UK EMIR RTS articles 12 and 13; and

(*2*) The Covered Entity applies substituted compliance for the requirements of Exchange Act section 15F(e) and Exchange Act rules 18a–1 through 18a–1d pursuant to this Order.

(6) *Daily Trading Records.* The requirements of Exchange Act section 15F(g), provided that the Covered Entity is subject to and complies with the requirements of PRA Fundamental Rules 2 and 6; FCA PRIN 2.1.1.R(2) and (3); PRA Recordkeeping Rule 2.1; FCA SYSC 9.1.1AR; and MiFID Org Reg article 21(1)(f), 21(4), and 72(1).

(7) *Examination and Production of Records.* Notwithstanding the forgoing provisions of paragraph (f) of this Order, this Order does not extend to, and Covered Entities remain subject to, the requirement of Exchange Act section 15F(f) to keep books and records open to inspection by any representative of the Commission and the requirement of Exchange Act rule 18a–6(g) to furnish promptly to a representative of the Commission legible, true, complete, and current copies of those records of the Covered Entity that are required to be preserved under Exchange Act rule 18a–6, or any other records of the Covered Entity that are subject to examination or required to be made or maintained pursuant to Exchange Act section 15F that are requested by a representative of the Commission.

(8) *English Translations.* Notwithstanding the forgoing provisions of paragraph (f) of this Order, to the extent documents are not prepared in the English language, Covered Entities must promptly furnish to a representative of the Commission upon request an English translation of any record, report, or notification of the Covered Entity that is required to be made, preserved, filed, or subject to examination pursuant to Exchange Act section 15F of this Order.

(g) Definitions

(1) ''Covered Entity'' means an entity that:

(i) Is a security-based swap dealer or major security-based swap participant registered with the Commission;

(ii) Is not a ''U.S. person,'' as that term is defined in rule 3a71–3(a)(4) under the Exchange Act;

(iii) Is a ''MiFID investment firm'' or ''third country investment firm,'' as such terms are defined in the FCA Handbook Glossary, that has permission from the FCA or PRA under Part 4A of FSMA to carry on regulated activities relating to investment services and activities in the United Kingdom; and

(iv) Is supervised by the FCA under the fixed supervision model and, if the firm is a PRA-authorized person, also supervised by the PRA as a Category 1 firm.

(2) ''Capital Requirements Regulations 2013'' means the UK Capital Requirements Regulations 2013, as amended from time to time.

(3) ''Companies Act'' means the UK Companies Act 2006, as amended from time to time.

(4) ''FCA'' means the UK's Financial Conduct Authority.

(5) ''FCA BIPRU'' means the Prudential Sourcebook for Banks, Building Societies and Investment Firms of the FCA Handbook, as amended from time to time.

(6) ''FCA CASS'' means the Client Asset Sourcebook of the FCA Handbook, as amended from time to time.

(7) ''FCA COBS'' means the Conduct of Business Sourcebook of the FCA Handbook, as amended from time to time.

(8) ''FCA COND'' means the Threshold Conditions of the FCA Handbook, as amended from time to time.

(9) ''FCA Enforcement Guide'' means the Enforcement Guide of the FCA Handbook, as amended from time to time.

(10) ''FCA FCG'' means the Financial Crime Guide of the FCA Handbook, as amended from time to time.

(11) ''FCA FIT'' means the Fit and Proper Test for Employees and Senior Personnel Sourcebook of the FCA Handbook, as amended from time to time.

(12) ''FCA Handbook'' means the FCA's Handbook of rules and guidance, as amended from time to time.

(13) ''FCA Handbook Glossary'' means the Glossary part of the FCA's Handbook of rules and guidance, as amended from time to time.

(14) ''FCA IFPRU'' means the Prudential Sourcebook for Investment Firms of the FCA Handbook, as amended from time to time.

(15) ''FCA PRIN'' means the Principles for Businesses Sourcebook of the FCA Handbook, as amended from time to time.

(16) ''FCA PROD'' means the Product Intervention and Product Governance Sourcebook of the FCA Handbook, as amended from time to time.

(17) ''FCA SUP'' means the Supervision Sourcebook of the FCA Handbook, as amended from time to time.

(18) ''FCA SYSC'' means the Senior Management Arrangements, Systems and Controls Sourcebook of the FCA Handbook, as amended from time to time.

(19) ''FSMA'' means the UK's Financial Services and Markets Act 2000, as amended from time to time.

(20) ''ICVC'' means investment company with variable capital as defined in the FCA Handbook Glossary.

(21) ''MLR 2017'' means the UK's Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017, as amended from time to time.

(22) ''PRA'' means the UK's Prudential Regulation Authority.

(23) ''PRA Capital Buffer Rules'' means the Capital Buffer Part of the PRA Rulebook for CRR Firms, as amended from time to time.

(24) ''PRA Certification Rules'' means the Certification Part of the PRA Rulebook for CRR Firms, as amended from time to time.

(25) ''PRA Definition of Capital Rules'' means the Definition of Capital Part of the PRA Rulebook for CRR Firms, as amended from time to time.

(26) ''PRA Fitness and Proprietary Rules'' means the Fitness and Propriety Part of the PRA Rulebook for CRR Firms, as amended from time to time.

(27) ''PRA Fundamental Rules'' means the Fundamental Rules Part of the PRA Rulebook for CRR Firms, as amended from time to time.

(28) ''PRA General Organisational Requirements'' means the General Organisational Requirements Part of the PRA Rulebook for CRR Firms, as amended from time to time.

(29) ''PRA Internal Capital Adequacy Assessment Rules'' means the Internal Capital Adequacy Assessment Part of the PRA Rulebook for CRR Firms, as amended from time to time.

(30) ''PRA Internal Liquidity Adequacy Assessment Rules'' means the Internal Liquidity Adequacy Assessment Part of the PRA Rulebook for CRR Firms, as amended from time to time.

(31) ''PRA Liquidity Coverage Requirement—UK Designated Investment Firms Rules'' means the PRA Liquidity Coverage Requirement—UK Designated Investment Firms Part of the PRA Rulebook for CRR Firms, as amended from time to time.

(32) ''PRA Notifications Rules'' means the Notifications Part of the PRA Rulebook for CRR Firms, as amended from time to time.

(33) ''PRA Outsourcing Rules'' means the Outsourcing Part of the PRA Rulebook for CRR Firms, as amended from time to time.

(34) ''PRA Recordkeeping Rules'' means the Recordkeeping Part of the PRA Rulebook for CRR Firms, as amended from time to time.

(35) ''PRA Regulatory Reporting Rules'' means the Regulatory Reporting Part of the PRA Rulebook for CRR Firms, as amended from time to time.

(36) ''PRA Remuneration Rules'' means the Remuneration Part of the PRA Rulebook for CRR Firms, as amended from time to time.

(37) ''PRA Risk Control Rules'' means the Risk Control Part of the PRA Rulebook for CRR Firms, as amended from time to time.

(38) ''PRA Rulebook'' or ''PRA Rulebook for CRR Firms'' means the PRA's Rulebook for Capital Requirement Regulation Firms, as amended from time to time.

(39) ''PRA Rulebook Glossary'' means the Glossary part of the PRA Rulebook for CRR Firms, as amended from time to time.

(40) ''PRA Senior Management Functions Rules'' means the Senior Management Functions Part of the PRA Rulebook for CRR Firms, as amended from time to time.

(41) ''Prudentially regulated'' means a Covered Entity that has a ''prudential regulator'' as that term is defined in Exchange Act section 3(a)(74).

(42) ''SMR'' means the Senior Managers Regime that forms part of the Senior Managers and Certification Regime, as amended from time to time.

(43) ''UK'' means the United Kingdom.

(44) ''UK CRR'' means the UK version of Regulation (EU) No 575/2013, as amended from time to time.

(45) ''UK CRR Reporting ITS'' means the UK version of Commission Implementing Regulation (EU) 680/2014.

(46) ''UK EMIR'' means the UK version of the ''European Market Infrastructure Regulation,'' Regulation (EU) No 648/2012, as amended from time to time.

(47) ''UK EMIR Margin RTS'' means the UK version of Commission Delegated Regulation (EU) 2016/2251, as amended from time to time.

(48) ''UK EMIR RTS'' means UK version of Commission Delegated Regulation (EU) No 149/2013, as amended from time to time.

(49) ''UK MAR'' means the UK version of Market Abuse Regulation (EU) 596/2014, as amended from time to time.

(50) ''UK MAR Investment Recommendations Regulation'' means the UK version of Commission Delegated Regulation (EU) 2016/958, as amended from time to time.

(51) ''UK MiFID Org Reg'' means the UK version of Commission Delegated Regulation (EU) 2017/565, as amended from time to time.

(52) ''UK MiFIR'' means the UK version of the ''Markets in Financial Instruments Regulation,'' Regulation (EU) 600/2014, as amended from time to time.

(53) ''UK Regulated Activities Order'' means the Financial Services and Markets Act 2000 (Regulated Activities) Order (SI 2001/544), as amended from time to time.

By the Commission.

Vanessa A. Countryman,

Secretary.

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