

BUSINESS RISK MITIGATION AND PRICE STABILIZATION
ACT OF 2013

JUNE 12, 2013.—Committed to the Committee of the Whole House on the State of
the Union and ordered to be printed

Mr. LUCAS, from the Committee on Agriculture,
submitted the following

R E P O R T

[To accompany H.R. 634]

[Including cost estimate of the Congressional Budget Office]

The Committee on Agriculture, to whom was referred the bill (H.R. 634) to provide end user exemptions from certain provisions of the Commodity Exchange Act and the Securities Exchange Act of 1934, and for other purposes, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

BRIEF EXPLANATION

The bill amends Section 4s(e) of the Commodity Exchange Act (CEA) as added by Section 731 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (P.L. 111-203) (the Dodd-Frank Act) to provide an explicit exemption from margin requirements for swap transactions involving end-users that qualify for the clearing exception under 2(h)(7)(A). The bill includes mirroring provisions to Section 15F(e) of the Securities Exchange Act of 1934 with respect to security-based swap transactions.

PURPOSE AND NEED

“End-users” are thousands of companies across the United States who utilize derivatives to hedge risks associated with their day-to-day operations, such as fluctuations in the prices of raw materials. Because these businesses do not pose systemic risk, Congress intended that the Dodd-Frank Act provide certain exemptions for end-users to ensure they were not unduly burdened by new margin

and capital requirements associated with their derivatives trades that would hamper their ability to expand and create jobs.

Indeed, Title VII of the Dodd-Frank Act includes an exemption for non-financial end-users from centrally clearing their derivatives trades. This exemption permits end-users to continue trading directly with a counterparty, (also known as trading “bilaterally,” or over-the-counter (OTC)) which means their swaps are negotiated privately between two parties and they are not executed and cleared using an exchange or clearinghouse. Generally, it is common for non-financial end-users, such as manufacturers, to avoid posting cash margin for their OTC derivative trades. End-users generally will not post margin because they are able to negotiate such terms with their counterparties due to the strength of their own balance sheet or by posting non-cash collateral, such as physical property. End-users typically seek to preserve their cash and liquid assets for reinvestment in their businesses. In recognition of this common practice, the Dodd-Frank Act included an exemption from margin requirements for end-users for OTC trades.

Section 731 of the Dodd-Frank Act (and Section 764 with respect to security-based swaps) requires margin requirements be applied to swap dealers and major swap participants for swaps that are not centrally cleared. For swap dealers and major swap participants that are banks, the prudential banking regulators (such as the Federal Reserve or Federal Deposit Insurance Corporation) are required to set the margin requirements. For swap dealers and major swap participants that are not banks, the U.S. Commodity Futures Trading Commission (CFTC) is required to set the margin requirements. Both the CFTC and the banking regulators have issued their own rule proposals establishing margin requirements pursuant to Sections 731 and 764.

Following the enactment of the Dodd-Frank Act in July of 2010, uncertainty arose regarding whether this provision permitted the regulators to impose margin requirements on swap dealers when they trade with end-users, which could then result in either a direct or indirect margin requirement on end-users. Subsequently, the principal authors of the Dodd-Frank Act, Senators Blanche Lincoln and Chris Dodd sent a letter to then-Chairmen Barney Frank and Collin Peterson to set forth and clarify congressional intent, stating:

The legislation does not authorize the regulators to impose margin on end users, those exempt entities that use swaps to hedge or mitigate commercial risk. If regulators raise the costs of end user transactions, they may create more risk. It is imperative that the regulators do not unnecessarily divert working capital from our economy into margin accounts, in a way that would discourage hedging by end users or impair economic growth. (Available at <http://agriculture.house.gov/pdf/letters/HouseSenateEndUserLetter.pdf>)

In addition, statements in the legislative history of sections 731 and 764 suggest that Congress did not intend, in enacting these sections, to impose margin requirements on nonfinancial end users engaged in hedging activities, even in cases where they entered into swaps or security-based swaps with swap entities.

In the CFTC's proposed rule on margin, it does not require margin for un-cleared swaps when non-bank swap dealers transact with non-financial end-users. However, the prudential banking regulators proposed rules would require margin be posted by non-financial end-users above certain established thresholds when they trade with swap dealers that are banks. Many of end-users' transactions occur with swap dealers that are banks, so the banking regulators' proposed rule is most relevant, and therefore of most concern, to end-users.

By the prudential banking regulators' own terms, their proposal to require margin stems directly from what they view to be a legal obligation under Title VII. The plain language of sections 731 and 764 provides that the Agencies adopt rules for covered swap entities imposing margin requirements on all non-cleared swaps. Despite clear congressional intent, those sections do not, by their terms, exclude a swap with a counterparty that is a commercial end-user. By providing an explicit exemption under Title VII through enactment of H.R. 634, the Agencies will no longer have a perceived legal obligation, and the congressional intent they acknowledge in their proposed rule will be implemented.

SECTION-BY-SECTION

Section 1 is the short title of the bill.

Section 2(a) amends section 4s(e) (registration and regulation of swap dealers and major swap participants) of the Commodity Exchange Act (CEA) by adding a new paragraph clarifying that the margin and capital requirements do not apply to transactions in which one of the parties qualify for the end user exemption to the clearing requirement in 2(h)(7)(A) or treatment of affiliates in 2(h)(7)(D).

Section 2(b) contains a similar amendment to the Securities Exchange Act.

Section 3 provides for expedited implementation of this act.

COMMITTEE CONSIDERATION

I. HEARINGS

In the 113th Congress, the Full Committee held a hearing March 14, 2013, to examine legislative improvements to Title VII of the Dodd-Frank Act which included H.R. 634, the Business Risk Mitigation and Price Stabilization Act of 2013. During the hearing, the Committee heard testimony from the Chairman of the U.S. Commodity Futures Trading Commission and six additional witnesses representing a broad spectrum of participants in the derivatives market.

Included was testimony from Jim Colby, Assistant Treasurer, Honeywell International Inc., who testified to the importance of the legislation:

“Honeywell is truly a global company, with more than 50 percent of our sales outside of the United States and we are therefore exposed to market risks from changes in interest rates, foreign exchange rates and commodity prices. When appropriate, we hedge exposures through the use of derivative contracts. The purpose of our hedging activities

is to eliminate risks that we cannot control, allowing us to focus on our core strengths, namely delivering high-quality products, on time, to our customers in a manner that not only meets, but exceeds expectations. We do not use derivatives for speculative purposes.

Today I will focus on the margin bill, as it is of particular interest to Honeywell. In approving the Dodd-Frank Act, Congress made clear that end-users were not to be subject to margin requirements. Nonetheless, regulations proposed by the Prudential Banking Regulators could require end-users to post margin. This stems directly from what they view to be a legal obligation under Title VII. While the regulations proposed by the CFTC are preferable, they do not provide end-users with the certainty that legislation offers. According to a Coalition for Derivatives End Users survey, a 3% initial margin requirement could reduce capital spending by as much as \$5.1 to \$6.7 billion among S&P 500 companies alone and cost 100,000 to 130,000 jobs.

To shed some light on Honeywell's potential exposure to margin requirements, we had approximately \$2 billion of hedging contracts outstanding at year-end that would be defined as a swap under Dodd-Frank. Applying 3% initial margin and 10% variation margin implies a potential margin requirement of \$260 million. Cash deposited in a margin account cannot be productively deployed in our businesses and therefore detracts from Honeywell's financial performance and ability to promote economic growth and protect American jobs."

II. BUSINESS MEETINGS

The Committee on Agriculture met, pursuant to notice, with a quorum present, on March 20, 2013, to consider H.R. 634, the Business Risk Mitigation and Price Stabilization Act of 2013, and other pending business.

By unanimous consent, the Subcommittee on General Farm Commodities and Risk Management was discharged from further consideration of H.R. 634, and the bill was placed before the Committee for consideration. Without objection, a first reading of the bill was waived and it was open for amendment at any point.

Chairman Lucas, Mr. Peterson, Mr. Austin Scott and Mr. McIntyre were recognized for statements, and then Counsel was recognized for a brief explanation of the bill. Following, Mr. Fincher was recognized to offer an amendment to H.R. 634 and Mr. McIntyre reserved a point of order against the amendment. Mr. Fincher then explained his amendment requiring the Financial Stability Oversight Committee to conduct a study of the impact of implementation of the Credit Valuation Adjustment capital requirement on U.S. customers, end users, and U.S. financial institutions. However, Mr. Fincher ultimately withdrew the amendment and Mr. McIntyre withdrew his point of order.

There being no other amendments, Mr. Peterson was recognized to offer a motion. By voice vote, the Peterson motion that the bill H.R. 634 be reported favorably to the House with recommendation that it do pass, was approved.

The Committee then continued with other pending business, and at the conclusion of the meeting, Chairman Lucas advised Members that pursuant to the rules of the House of Representatives Members had 2 calendar days to file any supplemental or minority views with the Committee.

Without objection, staff was given permission to make any necessary clerical, technical or conforming changes to reflect the intent of the Committee. Chairman Lucas thanked all the Members and adjourned the meeting.

COMMITTEE VOTES

In compliance with clause 3(b) of rule XIII of the House of Representatives, H.R. 634 was reported by voice vote with a majority quorum present. There was no request for a recorded vote.

COMMITTEE OVERSIGHT FINDINGS

Pursuant to clause 3(c)(1) of rule XIII of the Rules of the House of Representatives, the Committee on Agriculture's oversight findings and recommendations are reflected in the body of this report.

BUDGET ACT COMPLIANCE (SECTIONS 308, 402, AND 423)

The provisions of clause 3(c)(2) of rule XIII of the Rules of the House of Representatives and section 308(a)(1) of the Congressional Budget Act of 1974 (relating to estimates of new budget authority, new spending authority, new credit authority, or increased or decreased revenues or tax expenditures) are not considered applicable. The estimate and comparison required to be prepared by the Director of the Congressional Budget Office under clause 3(c)(3) of rule XIII of the Rules of the House of Representatives and sections 402 and 423 of the Congressional Budget Act of 1974 submitted to the Committee prior to the filing of this report are as follows:

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
Washington, DC, April 11, 2013.

Hon. FRANK D. LUCAS,
*Chairman, Committee on Agriculture,
House of Representatives, Washington, DC.*

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for H.R. 634, the Business Risk Mitigation and Price Stabilization Act of 2013.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Susan Willie.

Sincerely,

DOUGLAS W. ELMENDORF.

Enclosure.

H.R. 634—Business Risk Mitigation and Price Stabilization Act of 2013

H.R. 634 would exempt nonfinancial entities that enter into a swap or a security-based swap transaction from meeting certain margin requirements when the transaction is designed to offset losses or gains in other investments. (A swap is a contract that

calls for an exchange of cash between two participants, based on an underlying rate or index or on the performance of an asset.)

Both the Commodity Futures Trading Commission (CFTC) and the Securities and Exchange Commission (SEC) are developing regulations relating to margin requirements (minimum amounts of collateral that must be deposited, often with a broker or exchange, to cover some or all of the risk of a counterparty) in swap transactions as the result of the enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Public Law 111–203). In addition, other financial regulators, including the Federal Reserve System, the Office of the Comptroller of the Currency (OCC), and the Federal Deposit Insurance Corporation (FDIC) among others, are also developing margin requirements that would apply to the entities they regulate. Final regulations have not been completed by any agency.

Based on information from several of the affected agencies, CBO expects that incorporating the provisions of H.R. 634 at this point in the regulatory process would not require a significant increase in the workload of any agency. CBO estimates that any change in discretionary spending by the SEC and CFTC to implement the legislation would not be significant. Further, under current law, the SEC is authorized to collect fees sufficient to offset its appropriation each year. Therefore, we estimate that the net cost to the SEC would be negligible, assuming appropriation actions consistent with that authority.

Enacting H.R. 634 would affect direct spending and revenues; therefore, pay-as-you-go procedures apply. CBO expects that workloads for affected financial regulators (the Federal Reserve System, FDIC, and OCC among others) would not be significantly affected by the new requirements, and thus, we estimate that the effect on direct spending and revenues would be insignificant.

H.R. 634 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act and would impose no costs on state, local, or tribal governments.

The CBO staff contact for this estimate is Susan Willie. The estimate was approved by Theresa Gullo, Deputy Assistant Director for Budget Analysis.

PERFORMANCE GOALS AND OBJECTIVES

With respect to the requirement of clause 3(c)(4) of rule XIII of the Rules of the House of Representatives, the performance goals and objections of this legislation are to clarify congressional intent by providing an explicit exemption from margin requirements for swap transactions involving end-users that qualify for the end-user clearing exemption.

COMMITTEE COST ESTIMATE

Pursuant to clause 3(d)(2) of rule XIII of the Rules of the House of Representatives, the Committee report incorporates the cost estimate prepared by the Director of the Congressional Budget Office pursuant to sections 402 and 423 of the Congressional Budget Act of 1974.

ADVISORY COMMITTEE STATEMENT

No advisory committee within the meaning of section 5(b) of the Federal Advisory Committee Act was created by this legislation.

APPLICABILITY TO THE LEGISLATIVE BRANCH

The Committee finds that the legislation does not relate to the terms and conditions of employment or access to public services or accommodations within the meaning of section 102(b)(3) of the Congressional Accountability Act (Public Law 104–1).

FEDERAL MANDATES STATEMENT

The Committee adopted as its own, the estimate of Federal mandates prepared by the Director of the Congressional Budget Office pursuant to section 423 of the Unfunded Mandates Reform Act (Public Law 104–4).

EARMARK STATEMENT REQUIRED BY CLAUSE 9 OF RULE XXI OF THE
RULES OF HOUSE OF REPRESENTATIVES

H.R. 634 does not contain any congressional earmarks, limited tax benefits, or limited tariff benefits as defined in clause 9(e), 9(f), or 9(g) of rule XXI of the Rules of the House Representatives.

DUPLICATION OF FEDERAL PROGRAMS

H.R. 634 does not establish or reauthorize a program of the Federal Government known to be duplicative of another Federal program, a program that was included in any report from the Government Accountability Office to Congress pursuant to section 21 of Public Law 111–139, or any related program identified in the most recent Catalog of Federal Domestic Assistance.

DISCLOSURE OF DIRECTED RULE MAKINGS

The Committee does not believe that the legislation directs an executive branch official to conduct any specific rule making proceedings within the meaning of 5 U.S.C. 551.

CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3(e) of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, existing law in which no change is proposed is shown in roman):

COMMODITY EXCHANGE ACT

* * * * *

**SEC. 4s. REGISTRATION AND REGULATION OF SWAP DEALERS AND
MAJOR SWAP PARTICIPANTS.**

(a) REGISTRATION.—

(1) SWAP DEALERS.—It shall be unlawful for any person to act as a swap dealer unless the person is registered as a swap dealer with the Commission.

- (2) MAJOR SWAP PARTICIPANTS.—It shall be unlawful for any person to act as a major swap participant unless the person is registered as a major swap participant with the Commission.
- (b) REQUIREMENTS.—
- (1) IN GENERAL.—A person shall register as a swap dealer or major swap participant by filing a registration application with the Commission.
- (2) CONTENTS.—
- (A) IN GENERAL.—The application shall be made in such form and manner as prescribed by the Commission, and shall contain such information, as the Commission considers necessary concerning the business in which the applicant is or will be engaged.
- (B) CONTINUAL REPORTING.—A person that is registered as a swap dealer or major swap participant shall continue to submit to the Commission reports that contain such information pertaining to the business of the person as the Commission may require.
- (3) EXPIRATION.—Each registration under this section shall expire at such time as the Commission may prescribe by rule or regulation.
- (4) RULES.—Except as provided in subsections (d) and (e), the Commission may prescribe rules applicable to swap dealers and major swap participants, including rules that limit the activities of swap dealers and major swap participants.
- (5) TRANSITION.—Rules under this section shall provide for the registration of swap dealers and major swap participants not later than 1 year after the date of enactment of the Wall Street Transparency and Accountability Act of 2010.
- (6) STATUTORY DISQUALIFICATION.—Except to the extent otherwise specifically provided by rule, regulation, or order, it shall be unlawful for a swap dealer or a major swap participant to permit any person associated with a swap dealer or a major swap participant who is subject to a statutory disqualification to effect or be involved in effecting swaps on behalf of the swap dealer or major swap participant, if the swap dealer or major swap participant knew, or in the exercise of reasonable care should have known, of the statutory disqualification.
- (c) DUAL REGISTRATION.—
- (1) SWAP DEALER.—Any person that is required to be registered as a swap dealer under this section shall register with the Commission regardless of whether the person also is a depository institution or is registered with the Securities and Exchange Commission as a security-based swap dealer.
- (2) MAJOR SWAP PARTICIPANT.—Any person that is required to be registered as a major swap participant under this section shall register with the Commission regardless of whether the person also is a depository institution or is registered with the Securities and Exchange Commission as a major security-based swap participant.
- (d) RULEMAKINGS.—
- (1) IN GENERAL.—The Commission shall adopt rules for persons that are registered as swap dealers or major swap participants under this section.
- (2) EXCEPTION FOR PRUDENTIAL REQUIREMENTS.—

(A) IN GENERAL.—The Commission may not prescribe rules imposing prudential requirements on swap dealers or major swap participants for which there is a prudential regulator.

(B) APPLICABILITY.—Subparagraph (A) does not limit the authority of the Commission to prescribe rules as directed under this section.

(e) CAPITAL AND MARGIN REQUIREMENTS.—

(1) IN GENERAL.—

(A) SWAP DEALERS AND MAJOR SWAP PARTICIPANTS THAT ARE BANKS.—Each registered swap dealer and major swap participant for which there is a prudential regulator shall meet such minimum capital requirements and minimum initial and variation margin requirements as the prudential regulator shall by rule or regulation prescribe under paragraph (2)(A).

(B) SWAP DEALERS AND MAJOR SWAP PARTICIPANTS THAT ARE NOT BANKS.—Each registered swap dealer and major swap participant for which there is not a prudential regulator shall meet such minimum capital requirements and minimum initial and variation margin requirements as the Commission shall by rule or regulation prescribe under paragraph (2)(B).

(2) RULES.—

(A) SWAP DEALERS AND MAJOR SWAP PARTICIPANTS THAT ARE BANKS.—The prudential regulators, in consultation with the Commission and the Securities and Exchange Commission, shall jointly adopt rules for swap dealers and major swap participants, with respect to their activities as a swap dealer or major swap participant, for which there is a prudential regulator imposing—

(i) capital requirements; and

(ii) both initial and variation margin requirements on all swaps that are not cleared by a registered derivatives clearing organization.

(B) SWAP DEALERS AND MAJOR SWAP PARTICIPANTS THAT ARE NOT BANKS.—The Commission shall adopt rules for swap dealers and major swap participants, with respect to their activities as a swap dealer or major swap participant, for which there is not a prudential regulator imposing—

(i) capital requirements; and

(ii) both initial and variation margin requirements on all swaps that are not cleared by a registered derivatives clearing organization.

(C) CAPITAL.—In setting capital requirements for a person that is designated as a swap dealer or a major swap participant for a single type or single class or category of swap or activities, the prudential regulator and the Commission shall take into account the risks associated with other types of swaps or classes of swaps or categories of swaps engaged in and the other activities conducted by that person that are not otherwise subject to regulation applicable to that person by virtue of the status of the person as a swap dealer or a major swap participant.

(3) STANDARDS FOR CAPITAL AND MARGIN.—

(A) IN GENERAL.—To offset the greater risk to the swap dealer or major swap participant and the financial system arising from the use of swaps that are not cleared, the requirements imposed under paragraph (2) shall—

- (i) help ensure the safety and soundness of the swap dealer or major swap participant; and
- (ii) be appropriate for the risk associated with the non-cleared swaps held as a swap dealer or major swap participant.

(B) RULE OF CONSTRUCTION.—

(i) IN GENERAL.—Nothing in this section shall limit, or be construed to limit, the authority—

(I) of the Commission to set financial responsibility rules for a futures commission merchant or introducing broker registered pursuant to section 4f(a) (except for section 4f(a)(3)) in accordance with section 4f(b); or

(II) of the Securities and Exchange Commission to set financial responsibility rules for a broker or dealer registered pursuant to section 15(b) of the Securities Exchange Act of 1934 (15 U.S.C. 78o(b)) (except for section 15(b)(11) of that Act (15 U.S.C. 78o(b)(11)) in accordance with section 15(c)(3) of the Securities Exchange Act of 1934 (15 U.S.C. 78o(c)(3)).

(ii) FUTURES COMMISSION MERCHANTS AND OTHER DEALERS.—A futures commission merchant, introducing broker, broker, or dealer shall maintain sufficient capital to comply with the stricter of any applicable capital requirements to which such futures commission merchant, introducing broker, broker, or dealer is subject to under this Act or the Securities Exchange Act of 1934 (15 U.S.C. 78a et seq.).

(C) MARGIN REQUIREMENTS.—In prescribing margin requirements under this subsection, the prudential regulator with respect to swap dealers and major swap participants for which it is the prudential regulator and the Commission with respect to swap dealers and major swap participants for which there is no prudential regulator shall permit the use of noncash collateral, as the regulator or the Commission determines to be consistent with—

- (i) preserving the financial integrity of markets trading swaps; and
- (ii) preserving the stability of the United States financial system.

(D) COMPARABILITY OF CAPITAL AND MARGIN REQUIREMENTS.—

(i) IN GENERAL.—The prudential regulators, the Commission, and the Securities and Exchange Commission shall periodically (but not less frequently than annually) consult on minimum capital requirements and minimum initial and variation margin requirements.

(ii) COMPARABILITY.—The entities described in clause (i) shall, to the maximum extent practicable, es-

establish and maintain comparable minimum capital requirements and minimum initial and variation margin requirements, including the use of non cash collateral, for—

- (I) swap dealers; and
- (II) major swap participants.

(4) *APPLICABILITY WITH RESPECT TO COUNTERPARTIES.*—*The requirements of paragraphs (2)(A)(ii) and (2)(B)(ii) shall not apply to a swap in which a counterparty qualifies for an exception under section 2(h)(7)(A) or satisfies the criteria in section 2(h)(7)(D).*

(f) **REPORTING AND RECORDKEEPING.**—

(1) **IN GENERAL.**—Each registered swap dealer and major swap participant—

(A) shall make such reports as are required by the Commission by rule or regulation regarding the transactions and positions and financial condition of the registered swap dealer or major swap participant;

(B)(i) for which there is a prudential regulator, shall keep books and records of all activities related to the business as a swap dealer or major swap participant in such form and manner and for such period as may be prescribed by the Commission by rule or regulation; and

(ii) for which there is no prudential regulator, shall keep books and records in such form and manner and for such period as may be prescribed by the Commission by rule or regulation;

(C) shall keep books and records described in subparagraph (B) open to inspection and examination by any representative of the Commission; and

(D) shall keep any such books and records relating to swaps defined in section 1a(47)(A)(v) open to inspection and examination by the Securities and Exchange Commission.

(2) **RULES.**—The Commission shall adopt rules governing reporting and recordkeeping for swap dealers and major swap participants.

(g) **DAILY TRADING RECORDS.**—

(1) **IN GENERAL.**—Each registered swap dealer and major swap participant shall maintain daily trading records of the swaps of the registered swap dealer and major swap participant and all related records (including related cash or forward transactions) and recorded communications, including electronic mail, instant messages, and recordings of telephone calls, for such period as may be required by the Commission by rule or regulation.

(2) **INFORMATION REQUIREMENTS.**—The daily trading records shall include such information as the Commission shall require by rule or regulation.

(3) **COUNTERPARTY RECORDS.**—Each registered swap dealer and major swap participant shall maintain daily trading records for each counterparty in a manner and form that is identifiable with each swap transaction.

(4) **AUDIT TRAIL.**—Each registered swap dealer and major swap participant shall maintain a complete audit trail for conducting comprehensive and accurate trade reconstructions.

(5) **RULES.**—The Commission shall adopt rules governing daily trading records for swap dealers and major swap participants.

(h) **BUSINESS CONDUCT STANDARDS.**—

(1) **IN GENERAL.**—Each registered swap dealer and major swap participant shall conform with such business conduct standards as prescribed in paragraph (3) and as may be prescribed by the Commission by rule or regulation that relate to—

(A) fraud, manipulation, and other abusive practices involving swaps (including swaps that are offered but not entered into);

(B) diligent supervision of the business of the registered swap dealer and major swap participant;

(C) adherence to all applicable position limits; and

(D) such other matters as the Commission determines to be appropriate.

(2) **RESPONSIBILITIES WITH RESPECT TO SPECIAL ENTITIES.**—

(A) **ADVISING SPECIAL ENTITIES.**—A swap dealer or major swap participant that acts as an advisor to a special entity regarding a swap shall comply with the requirements of subparagraph (4) with respect to such Special Entity.

(B) **ENTERING OF SWAPS WITH RESPECT TO SPECIAL ENTITIES.**—A swap dealer that enters into or offers to enter into swap with a Special Entity shall comply with the requirements of subparagraph (5) with respect to such Special Entity.

(C) **SPECIAL ENTITY DEFINED.**—For purposes of this subsection, the term “special entity” means—

(i) a Federal agency;

(ii) a State, State agency, city, county, municipality, or other political subdivision of a State;

(iii) any employee benefit plan, as defined in section 3 of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1002);

(iv) any governmental plan, as defined in section 3 of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1002); or

(v) any endowment, including an endowment that is an organization described in section 501(c)(3) of the Internal Revenue Code of 1986.

(3) **BUSINESS CONDUCT REQUIREMENTS.**—Business conduct requirements adopted by the Commission shall—

(A) establish a duty for a swap dealer or major swap participant to verify that any counterparty meets the eligibility standards for an eligible contract participant;

(B) require disclosure by the swap dealer or major swap participant to any counterparty to the transaction (other than a swap dealer, major swap participant, security-based swap dealer, or major security-based swap participant) of—

(i) information about the material risks and characteristics of the swap;

(ii) any material incentives or conflicts of interest that the swap dealer or major swap participant may have in connection with the swap; and

(iii)(I) for cleared swaps, upon the request of the counterparty, receipt of the daily mark of the transaction from the appropriate derivatives clearing organization; and

(II) for uncleared swaps, receipt of the daily mark of the transaction from the swap dealer or the major swap participant;

(C) establish a duty for a swap dealer or major swap participant to communicate in a fair and balanced manner based on principles of fair dealing and good faith; and

(D) establish such other standards and requirements as the Commission may determine are appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this Act.

(4) SPECIAL REQUIREMENTS FOR SWAP DEALERS ACTING AS ADVISORS.—

(A) IN GENERAL.—It shall be unlawful for a swap dealer or major swap participant—

(i) to employ any device, scheme, or artifice to defraud any Special Entity or prospective customer who is a Special Entity;

(ii) to engage in any transaction, practice, or course of business that operates as a fraud or deceit on any Special Entity or prospective customer who is a Special Entity; or

(iii) to engage in any act, practice, or course of business that is fraudulent, deceptive or manipulative.

(B) DUTY.—Any swap dealer that acts as an advisor to a Special Entity shall have a duty to act in the best interests of the Special Entity.

(C) REASONABLE EFFORTS.—Any swap dealer that acts as an advisor to a Special Entity shall make reasonable efforts to obtain such information as is necessary to make a reasonable determination that any swap recommended by the swap dealer is in the best interests of the Special Entity, including information relating to—

(i) the financial status of the Special Entity;

(ii) the tax status of the Special Entity;

(iii) the investment or financing objectives of the Special Entity; and

(iv) any other information that the Commission may prescribe by rule or regulation.

(5) SPECIAL REQUIREMENTS FOR SWAP DEALERS AS COUNTERPARTIES TO SPECIAL ENTITIES.—

(A) Any swap dealer or major swap participant that offers to enter or enters into a swap with a Special Entity shall—

(i) comply with any duty established by the Commission for a swap dealer or major swap participant, with respect to a counterparty that is an eligible contract

participant within the meaning of subclause (I) or (II) of clause (vii) of section 1a(18) of this Act, that requires the swap dealer or major swap participant to have a reasonable basis to believe that the counterparty that is a Special Entity has an independent representative that—

(I) has sufficient knowledge to evaluate the transaction and risks;

(II) is not subject to a statutory disqualification;

(III) is independent of the swap dealer or major swap participant;

(IV) undertakes a duty to act in the best interests of the counterparty it represents;

(V) makes appropriate disclosures;

(VI) will provide written representations to the Special Entity regarding fair pricing and the appropriateness of the transaction; and

(VII) in the case of employee benefit plans subject to the Employee Retirement Income Security act of 1974, is a fiduciary as defined in section 3 of that Act (29 U.S.C. 1002); and

(ii) before the initiation of the transaction, disclose to the Special Entity in writing the capacity in which the swap dealer is acting; and

(B) the Commission may establish such other standards and requirements as the Commission may determine are appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this Act.

(6) RULES.—The Commission shall prescribe rules under this subsection governing business conduct standards for swap dealers and major swap participants.

(7) APPLICABILITY.—This section shall not apply with respect to a transaction that is—

(A) initiated by a Special Entity on an exchange or swap execution facility; and

(B) one in which the swap dealer or major swap participant does not know the identity of the counterparty to the transaction.

(i) DOCUMENTATION STANDARDS.—

(1) IN GENERAL.—Each registered swap dealer and major swap participant shall conform with such standards as may be prescribed by the Commission by rule or regulation that relate to timely and accurate confirmation, processing, netting, documentation, and valuation of all swaps.

(2) RULES.—The Commission shall adopt rules governing documentation standards for swap dealers and major swap participants.

(j) DUTIES.—Each registered swap dealer and major swap participant at all times shall comply with the following requirements:

(1) MONITORING OF TRADING.—The swap dealer or major swap participant shall monitor its trading in swaps to prevent violations of applicable position limits.

(2) RISK MANAGEMENT PROCEDURES.—The swap dealer or major swap participant shall establish robust and professional

risk management systems adequate for managing the day-to-day business of the swap dealer or major swap participant.

(3) DISCLOSURE OF GENERAL INFORMATION.—The swap dealer or major swap participant shall disclose to the Commission and to the prudential regulator for the swap dealer or major swap participant, as applicable, information concerning—

- (A) terms and conditions of its swaps;
- (B) swap trading operations, mechanisms, and practices;
- (C) financial integrity protections relating to swaps; and
- (D) other information relevant to its trading in swaps.

(4) ABILITY TO OBTAIN INFORMATION.—The swap dealer or major swap participant shall—

- (A) establish and enforce internal systems and procedures to obtain any necessary information to perform any of the functions described in this section; and
- (B) provide the information to the Commission and to the prudential regulator for the swap dealer or major swap participant, as applicable, on request.

(5) CONFLICTS OF INTEREST.—The swap dealer and major swap participant shall implement conflict-of-interest systems and procedures that—

- (A) establish structural and institutional safeguards to ensure that the activities of any person within the firm relating to research or analysis of the price or market for any commodity or swap or acting in a role of providing clearing activities or making determinations as to accepting clearing customers are separated by appropriate informational partitions within the firm from the review, pressure, or oversight of persons whose involvement in pricing, trading, or clearing activities might potentially bias their judgment or supervision and contravene the core principles of open access and the business conduct standards described in this Act; and
- (B) address such other issues as the Commission determines to be appropriate.

(6) ANTITRUST CONSIDERATIONS.—Unless necessary or appropriate to achieve the purposes of this Act, a swap dealer or major swap participant shall not—

- (A) adopt any process or take any action that results in any unreasonable restraint of trade; or
- (B) impose any material anticompetitive burden on trading or clearing.

(7) RULES.—The Commission shall prescribe rules under this subsection governing duties of swap dealers and major swap participants.

(k) DESIGNATION OF CHIEF COMPLIANCE OFFICER.—

(1) IN GENERAL.—Each swap dealer and major swap participant shall designate an individual to serve as a chief compliance officer.

(2) DUTIES.—The chief compliance officer shall—

- (A) report directly to the board or to the senior officer of the swap dealer or major swap participant;
- (B) review the compliance of the swap dealer or major swap participant with respect to the swap dealer and

major swap participant requirements described in this section;

(C) in consultation with the board of directors, a body performing a function similar to the board, or the senior officer of the organization, resolve any conflicts of interest that may arise;

(D) be responsible for administering each policy and procedure that is required to be established pursuant to this section;

(E) ensure compliance with this Act (including regulations) relating to swaps, including each rule prescribed by the Commission under this section;

(F) establish procedures for the remediation of non-compliance issues identified by the chief compliance officer through any—

- (i) compliance office review;
- (ii) look-back;
- (iii) internal or external audit finding;
- (iv) self-reported error; or
- (v) validated complaint; and

(G) establish and follow appropriate procedures for the handling, management response, remediation, retesting, and closing of noncompliance issues.

(3) ANNUAL REPORTS.—

(A) IN GENERAL.—In accordance with rules prescribed by the Commission, the chief compliance officer shall annually prepare and sign a report that contains a description of—

- (i) the compliance of the swap dealer or major swap participant with respect to this Act (including regulations); and
- (ii) each policy and procedure of the swap dealer or major swap participant of the chief compliance officer (including the code of ethics and conflict of interest policies).

(B) REQUIREMENTS.—A compliance report under subparagraph (A) shall—

- (i) accompany each appropriate financial report of the swap dealer or major swap participant that is required to be furnished to the Commission pursuant to this section; and
- (ii) include a certification that, under penalty of law, the compliance report is accurate and complete.

(1) SEGREGATION REQUIREMENTS.—

(1) SEGREGATION OF ASSETS HELD AS COLLATERAL IN UNCLEARED SWAP TRANSACTIONS.—

(A) NOTIFICATION.—A swap dealer or major swap participant shall be required to notify the counterparty of the swap dealer or major swap participant at the beginning of a swap transaction that the counterparty has the right to require segregation of the funds or other property supplied to margin, guarantee, or secure the obligations of the counterparty.

(B) SEGREGATION AND MAINTENANCE OF FUNDS.—At the request of a counterparty to a swap that provides funds or

other property to a swap dealer or major swap participant to margin, guarantee, or secure the obligations of the counterparty, the swap dealer or major swap participant shall—

(i) segregate the funds or other property for the benefit of the counterparty; and

(ii) in accordance with such rules and regulations as the Commission may promulgate, maintain the funds or other property in a segregated account separate from the assets and other interests of the swap dealer or major swap participant.

(2) **APPLICABILITY.**—The requirements described in paragraph (1) shall—

(A) apply only to a swap between a counterparty and a swap dealer or major swap participant that is not submitted for clearing to a derivatives clearing organization; and

(B)(i) not apply to variation margin payments; or

(ii) not preclude any commercial arrangement regarding—

(I) the investment of segregated funds or other property that may only be invested in such investments as the Commission may permit by rule or regulation; and

(II) the related allocation of gains and losses resulting from any investment of the segregated funds or other property.

(3) **USE OF INDEPENDENT THIRD-PARTY CUSTODIANS.**—The segregated account described in paragraph (1) shall be—

(A) carried by an independent third-party custodian; and

(B) designated as a segregated account for and on behalf of the counterparty.

(4) **REPORTING REQUIREMENT.**—If the counterparty does not choose to require segregation of the funds or other property supplied to margin, guarantee, or secure the obligations of the counterparty, the swap dealer or major swap participant shall report to the counterparty of the swap dealer or major swap participant on a quarterly basis that the back office procedures of the swap dealer or major swap participant relating to margin and collateral requirements are in compliance with the agreement of the counterparties.

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SECURITIES EXCHANGE ACT OF 1934

TITLE I—REGULATION OF SECURITIES EXCHANGES

* * * * *

SEC. 15F. REGISTRATION AND REGULATION OF SECURITY-BASED SWAP DEALERS AND MAJOR SECURITY-BASED SWAP PARTICIPANTS.

(a) **REGISTRATION.**—

(1) **SECURITY-BASED SWAP DEALERS.**—It shall be unlawful for any person to act as a security-based swap dealer unless the

person is registered as a security-based swap dealer with the Commission.

(2) MAJOR SECURITY-BASED SWAP PARTICIPANTS.—It shall be unlawful for any person to act as a major security-based swap participant unless the person is registered as a major security-based swap participant with the Commission.

(b) REQUIREMENTS.—

(1) IN GENERAL.—A person shall register as a security-based swap dealer or major security-based swap participant by filing a registration application with the Commission.

(2) CONTENTS.—

(A) IN GENERAL.—The application shall be made in such form and manner as prescribed by the Commission, and shall contain such information, as the Commission considers necessary concerning the business in which the applicant is or will be engaged.

(B) CONTINUAL REPORTING.—A person that is registered as a security-based swap dealer or major security-based swap participant shall continue to submit to the Commission reports that contain such information pertaining to the business of the person as the Commission may require.

(3) EXPIRATION.—Each registration under this section shall expire at such time as the Commission may prescribe by rule or regulation.

(4) RULES.—Except as provided in subsections (d) and (e), the Commission may prescribe rules applicable to security-based swap dealers and major security-based swap participants, including rules that limit the activities of non-bank security-based swap dealers and major security-based swap participants.

(5) TRANSITION.—Not later than 1 year after the date of enactment of the Wall Street Transparency and Accountability Act of 2010, the Commission shall issue rules under this section to provide for the registration of security-based swap dealers and major security-based swap participants.

(6) STATUTORY DISQUALIFICATION.—Except to the extent otherwise specifically provided by rule, regulation, or order of the Commission, it shall be unlawful for a security-based swap dealer or a major security-based swap participant to permit any person associated with a security-based swap dealer or a major security-based swap participant who is subject to a statutory disqualification to effect or be involved in effecting security-based swaps on behalf of the security-based swap dealer or major security-based swap participant, if the security-based swap dealer or major security-based swap participant knew, or in the exercise of reasonable care should have known, of the statutory disqualification.

(c) DUAL REGISTRATION.—

(1) SECURITY-BASED SWAP DEALER.—Any person that is required to be registered as a security-based swap dealer under this section shall register with the Commission, regardless of whether the person also is registered with the Commodity Futures Trading Commission as a swap dealer.

(2) MAJOR SECURITY-BASED SWAP PARTICIPANT.—Any person that is required to be registered as a major security-based

swap participant under this section shall register with the Commission, regardless of whether the person also is registered with the Commodity Futures Trading Commission as a major swap participant.

(d) RULEMAKING.—

(1) IN GENERAL.— The Commission shall adopt rules for persons that are registered as security-based swap dealers or major security-based swap participants under this section.

(2) EXCEPTION FOR PRUDENTIAL REQUIREMENTS.—

(A) IN GENERAL.—The Commission may not prescribe rules imposing prudential requirements on security-based swap dealers or major security-based swap participants for which there is a prudential regulator.

(B) APPLICABILITY.—Subparagraph (A) does not limit the authority of the Commission to prescribe rules as directed under this section.

(e) CAPITAL AND MARGIN REQUIREMENTS.—

(1) IN GENERAL.—

(A) SECURITY-BASED SWAP DEALERS AND MAJOR SECURITY-BASED SWAP PARTICIPANTS THAT ARE BANKS.—Each registered security-based swap dealer and major security-based swap participant for which there is not a prudential regulator shall meet such minimum capital requirements and minimum initial and variation margin requirements as the prudential regulator shall by rule or regulation prescribe under paragraph (2)(A).

(B) SECURITY-BASED SWAP DEALERS AND MAJOR SECURITY-BASED SWAP PARTICIPANTS THAT ARE NOT BANKS.—Each registered security-based swap dealer and major security-based swap participant for which there is not a prudential regulator shall meet such minimum capital requirements and minimum initial and variation margin requirements as the Commission shall by rule or regulation prescribe under paragraph (2)(B).

(2) RULES.—

(A) SECURITY-BASED SWAP DEALERS AND MAJOR SECURITY-BASED SWAP PARTICIPANTS THAT ARE BANKS.—The prudential regulators, in consultation with the Commission and the Commodity Futures Trading Commission, shall adopt rules for security-based swap dealers and major security-based swap participants, with respect to their activities as a swap dealer or major swap participant, for which there is a prudential regulator imposing—

(i) capital requirements; and

(ii) both initial and variation margin requirements on all security-based swaps that are not cleared by a registered clearing agency.

(B) SECURITY-BASED SWAP DEALERS AND MAJOR SECURITY-BASED SWAP PARTICIPANTS THAT ARE NOT BANKS.—The Commission shall adopt rules for security-based swap dealers and major security-based swap participants, with respect to their activities as a swap dealer or major swap participant, for which there is not a prudential regulator imposing—

(i) capital requirements; and

(ii) both initial and variation margin requirements on all swaps that are not cleared by a registered clearing agency.

(C) CAPITAL.—In setting capital requirements for a person that is designated as a security-based swap dealer or a major security-based swap participant for a single type or single class or category of security-based swap or activities, the prudential regulator and the Commission shall take into account the risks associated with other types of security-based swaps or classes of security-based swaps or categories of security-based swaps engaged in and the other activities conducted by that person that are not otherwise subject to regulation applicable to that person by virtue of the status of the person.

(3) STANDARDS FOR CAPITAL AND MARGIN.—

(A) IN GENERAL.—To offset the greater risk to the security-based swap dealer or major security-based swap participant and the financial system arising from the use of security-based swaps that are not cleared, the requirements imposed under paragraph (2) shall —

(i) help ensure the safety and soundness of the security-based swap dealer or major security-based swap participant; and

(ii) be appropriate for the risk associated with the non-cleared security-based swaps held as a security-based swap dealer or major security-based swap participant.

(B) RULE OF CONSTRUCTION.—

(i) IN GENERAL.—Nothing in this section shall limit, or be construed to limit, the authority—

(I) of the Commission to set financial responsibility rules for a broker or dealer registered pursuant to section 15(b) (except for section 15(b)(11) thereof) in accordance with section 15(c)(3); or

(II) of the Commodity Futures Trading Commission to set financial responsibility rules for a futures commission merchant or introducing broker registered pursuant to section 4f(a) of the Commodity Exchange Act (except for section 4f(a)(3) thereof) in accordance with section 4f(b) of the Commodity Exchange Act.

(ii) FUTURES COMMISSION MERCHANTS AND OTHER DEALERS.—A futures commission merchant, introducing broker, broker, or dealer shall maintain sufficient capital to comply with the stricter of any applicable capital requirements to which such futures commission merchant, introducing broker, broker, or dealer is subject to under this title or the Commodity Exchange Act.

(C) MARGIN REQUIREMENTS.—In prescribing margin requirements under this subsection, the prudential regulator with respect to security-based swap dealers and major security-based swap participants that are depository institutions, and the Commission with respect to security-based swap dealers and major security-based swap participants

that are not depository institutions shall permit the use of noncash collateral, as the regulator or the Commission determines to be consistent with—

(i) preserving the financial integrity of markets trading security-based swaps; and

(ii) preserving the stability of the United States financial system.

(D) COMPARABILITY OF CAPITAL AND MARGIN REQUIREMENTS.—

(i) IN GENERAL.—The prudential regulators, the Commission, and the Securities and Exchange Commission shall periodically (but not less frequently than annually) consult on minimum capital requirements and minimum initial and variation margin requirements.

(ii) COMPARABILITY.—The entities described in clause (i) shall, to the maximum extent practicable, establish and maintain comparable minimum capital requirements and minimum initial and variation margin requirements, including the use of noncash collateral, for—

(I) security-based swap dealers; and

(II) major security-based swap participants.

(4) APPLICABILITY WITH RESPECT TO COUNTERPARTIES.—*The requirements of paragraphs (2)(A)(ii) and (2)(B)(ii) shall not apply to a security-based swap in which a counterparty qualifies for an exception under section 3C(g)(1) or satisfies the criteria in section 3C(g)(4).*

(f) REPORTING AND RECORDKEEPING.—

(1) IN GENERAL.—Each registered security-based swap dealer and major security-based swap participant—

(A) shall make such reports as are required by the Commission, by rule or regulation, regarding the transactions and positions and financial condition of the registered security-based swap dealer or major security-based swap participant;

(B)(i) for which there is a prudential regulator, shall keep books and records of all activities related to the business as a security-based swap dealer or major security-based swap participant in such form and manner and for such period as may be prescribed by the Commission by rule or regulation; and

(ii) for which there is no prudential regulator, shall keep books and records in such form and manner and for such period as may be prescribed by the Commission by rule or regulation; and

(C) shall keep books and records described in subparagraph (B) open to inspection and examination by any representative of the Commission.

(2) RULES.—The Commission shall adopt rules governing reporting and recordkeeping for security-based swap dealers and major security-based swap participants.

(g) DAILY TRADING RECORDS.—

(1) IN GENERAL.—Each registered security-based swap dealer and major security-based swap participant shall maintain daily

trading records of the security-based swaps of the registered security-based swap dealer and major security-based swap participant and all related records (including related cash or forward transactions) and recorded communications, including electronic mail, instant messages, and recordings of telephone calls, for such period as may be required by the Commission by rule or regulation.

(2) INFORMATION REQUIREMENTS.—The daily trading records shall include such information as the Commission shall require by rule or regulation.

(3) COUNTERPARTY RECORDS.—Each registered security-based swap dealer and major security-based swap participant shall maintain daily trading records for each counterparty in a manner and form that is identifiable with each security-based swap transaction.

(4) AUDIT TRAIL.—Each registered security-based swap dealer and major security-based swap participant shall maintain a complete audit trail for conducting comprehensive and accurate trade reconstructions.

(5) RULES.—The Commission shall adopt rules governing daily trading records for security-based swap dealers and major security-based swap participants.

(h) BUSINESS CONDUCT STANDARDS.—

(1) IN GENERAL.—Each registered security-based swap dealer and major security-based swap participant shall conform with such business conduct standards as prescribed in paragraph (3) and as may be prescribed by the Commission by rule or regulation that relate to—

(A) fraud, manipulation, and other abusive practices involving security-based swaps (including security-based swaps that are offered but not entered into);

(B) diligent supervision of the business of the registered security-based swap dealer and major security-based swap participant;

(C) adherence to all applicable position limits; and

(D) such other matters as the Commission determines to be appropriate.

(2) RESPONSIBILITIES WITH RESPECT TO SPECIAL ENTITIES.—

(A) ADVISING SPECIAL ENTITIES.—A security-based swap dealer or major security-based swap participant that acts as an advisor to special entity regarding a security-based swap shall comply with the requirements of paragraph (4) with respect to such special entity.

(B) ENTERING OF SECURITY-BASED SWAPS WITH RESPECT TO SPECIAL ENTITIES.—A security-based swap dealer that enters into or offers to enter into security-based swap with a special entity shall comply with the requirements of paragraph (5) with respect to such special entity.

(C) SPECIAL ENTITY DEFINED.—For purposes of this subsection, the term “special entity” means—

(i) a Federal agency;

(ii) a State, State agency, city, county, municipality, or other political subdivision of a State or;

(iii) any employee benefit plan, as defined in section 3 of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1002);

(iv) any governmental plan, as defined in section 3 of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1002); or

(v) any endowment, including an endowment that is an organization described in section 501(c)(3) of the Internal Revenue Code of 1986.

(3) BUSINESS CONDUCT REQUIREMENTS.—Business conduct requirements adopted by the Commission shall—

(A) establish a duty for a security-based swap dealer or major security-based swap participant to verify that any counterparty meets the eligibility standards for an eligible contract participant;

(B) require disclosure by the security-based swap dealer or major security-based swap participant to any counterparty to the transaction (other than a security-based swap dealer, major security-based swap participant, security-based swap dealer, or major security-based swap participant) of—

(i) information about the material risks and characteristics of the security-based swap;

(ii) any material incentives or conflicts of interest that the security-based swap dealer or major security-based swap participant may have in connection with the security-based swap; and

(iii)(I) for cleared security-based swaps, upon the request of the counterparty, receipt of the daily mark of the transaction from the appropriate derivatives clearing organization; and

(II) for uncleared security-based swaps, receipt of the daily mark of the transaction from the security-based swap dealer or the major security-based swap participant;

(C) establish a duty for a security-based swap dealer or major security-based swap participant to communicate in a fair and balanced manner based on principles of fair dealing and good faith; and

(D) establish such other standards and requirements as the Commission may determine are appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this Act.

(4) SPECIAL REQUIREMENTS FOR SECURITY-BASED SWAP DEALERS ACTING AS ADVISORS.—

(A) IN GENERAL.—It shall be unlawful for a security-based swap dealer or major security-based swap participant—

(i) to employ any device, scheme, or artifice to defraud any special entity or prospective customer who is a special entity;

(ii) to engage in any transaction, practice, or course of business that operates as a fraud or deceit on any special entity or prospective customer who is a special entity; or

(iii) to engage in any act, practice, or course of business that is fraudulent, deceptive, or manipulative.

(B) DUTY.—Any security-based swap dealer that acts as an advisor to a special entity shall have a duty to act in the best interests of the special entity.

(C) REASONABLE EFFORTS.—Any security-based swap dealer that acts as an advisor to a special entity shall make reasonable efforts to obtain such information as is necessary to make a reasonable determination that any security-based swap recommended by the security-based swap dealer is in the best interests of the special entity, including information relating to—

- (i) the financial status of the special entity;
- (ii) the tax status of the special entity;
- (iii) the investment or financing objectives of the special entity; and
- (iv) any other information that the Commission may prescribe by rule or regulation.

(5) SPECIAL REQUIREMENTS FOR SECURITY-BASED SWAP DEALERS AS COUNTERPARTIES TO SPECIAL ENTITIES.—

(A) IN GENERAL.—Any security-based swap dealer or major security-based swap participant that offers to or enters into a security-based swap with a special entity shall—

(i) comply with any duty established by the Commission for a security-based swap dealer or major security-based swap participant, with respect to a counterparty that is an eligible contract participant within the meaning of subclause (I) or (II) of clause (vii) of section 1a(18) of the Commodity Exchange Act, that requires the security-based swap dealer or major security-based swap participant to have a reasonable basis to believe that the counterparty that is a special entity has an independent representative that—

- (I) has sufficient knowledge to evaluate the transaction and risks;
- (II) is not subject to a statutory disqualification;
- (III) is independent of the security-based swap dealer or major security-based swap participant;
- (IV) undertakes a duty to act in the best interests of the counterparty it represents;
- (V) makes appropriate disclosures;
- (VI) will provide written representations to the special entity regarding fair pricing and the appropriateness of the transaction; and

(VII) in the case of employee benefit plans subject to the Employee Retirement Income Security Act of 1974, is a fiduciary as defined in section 3 of that Act (29 U.S.C. 1002); and

(ii) before the initiation of the transaction, disclose to the special entity in writing the capacity in which the security-based swap dealer is acting.

(B) COMMISSION AUTHORITY.—The Commission may establish such other standards and requirements under this paragraph as the Commission may determine are appro-

priate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of this Act.

(6) RULES.—The Commission shall prescribe rules under this subsection governing business conduct standards for security-based swap dealers and major security-based swap participants.

(7) APPLICABILITY.—This subsection shall not apply with respect to a transaction that is—

(A) initiated by a special entity on an exchange or security-based swaps execution facility; and

(B) the security-based swap dealer or major security-based swap participant does not know the identity of the counterparty to the transaction.”

(i) DOCUMENTATION STANDARDS.—

(1) IN GENERAL.—Each registered security-based swap dealer and major security-based swap participant shall conform with such standards as may be prescribed by the Commission, by rule or regulation, that relate to timely and accurate confirmation, processing, netting, documentation, and valuation of all security-based swaps.

(2) RULES.—The Commission shall adopt rules governing documentation standards for security-based swap dealers and major security-based swap participants.

(j) DUTIES.—Each registered security-based swap dealer and major security-based swap participant shall, at all times, comply with the following requirements:

(1) MONITORING OF TRADING.—The security-based swap dealer or major security-based swap participant shall monitor its trading in security-based swaps to prevent violations of applicable position limits.

(2) RISK MANAGEMENT PROCEDURES.—The security-based swap dealer or major security-based swap participant shall establish robust and professional risk management systems adequate for managing the day-to-day business of the security-based swap dealer or major security-based swap participant.

(3) DISCLOSURE OF GENERAL INFORMATION.—The security-based swap dealer or major security-based swap participant shall disclose to the Commission and to the prudential regulator for the security-based swap dealer or major security-based swap participant, as applicable, information concerning—

(A) terms and conditions of its security-based swaps;

(B) security-based swap trading operations, mechanisms, and practices;

(C) financial integrity protections relating to security-based swaps; and

(D) other information relevant to its trading in security-based swaps.

(4) ABILITY TO OBTAIN INFORMATION.—The security-based swap dealer or major security-based swap participant shall—

(A) establish and enforce internal systems and procedures to obtain any necessary information to perform any of the functions described in this section; and

(B) provide the information to the Commission and to the prudential regulator for the security-based swap dealer

or major security-based swap participant, as applicable, on request.

(5) CONFLICTS OF INTEREST.—The security-based swap dealer and major security-based swap participant shall implement conflict-of-interest systems and procedures that—

(A) establish structural and institutional safeguards to ensure that the activities of any person within the firm relating to research or analysis of the price or market for any security-based swap or acting in a role of providing clearing activities or making determinations as to accepting clearing customers are separated by appropriate informational partitions within the firm from the review, pressure, or oversight of persons whose involvement in pricing, trading, or clearing activities might potentially bias their judgment or supervision and contravene the core principles of open access and the business conduct standards described in this title; and

(B) address such other issues as the Commission determines to be appropriate.

(6) ANTITRUST CONSIDERATIONS.—Unless necessary or appropriate to achieve the purposes of this title, the security-based swap dealer or major security-based swap participant shall not—

(A) adopt any process or take any action that results in any unreasonable restraint of trade; or

(B) impose any material anticompetitive burden on trading or clearing.

(7) RULES.—The Commission shall prescribe rules under this subsection governing duties of security-based swap dealers and major security-based swap participants.

(k) DESIGNATION OF CHIEF COMPLIANCE OFFICER.—

(1) IN GENERAL.—Each security-based swap dealer and major security-based swap participant shall designate an individual to serve as a chief compliance officer.

(2) DUTIES.—The chief compliance officer shall—

(A) report directly to the board or to the senior officer of the security-based swap dealer or major security-based swap participant;

(B) review the compliance of the security-based swap dealer or major security-based swap participant with respect to the security-based swap dealer and major security-based swap participant requirements described in this section;

(C) in consultation with the board of directors, a body performing a function similar to the board, or the senior officer of the organization, resolve any conflicts of interest that may arise;

(D) be responsible for administering each policy and procedure that is required to be established pursuant to this section;

(E) ensure compliance with this title (including regulations) relating to security-based swaps, including each rule prescribed by the Commission under this section;

- (F) establish procedures for the remediation of non-compliance issues identified by the chief compliance officer through any—
- (i) compliance office review;
 - (ii) look-back;
 - (iii) internal or external audit finding;
 - (iv) self-reported error; or
 - (v) validated complaint; and
- (G) establish and follow appropriate procedures for the handling, management response, remediation, retesting, and closing of noncompliance issues.
- (3) ANNUAL REPORTS.—
- (A) IN GENERAL.—In accordance with rules prescribed by the Commission, the chief compliance officer shall annually prepare and sign a report that contains a description of—
- (i) the compliance of the security-based swap dealer or major swap participant with respect to this title (including regulations); and
 - (ii) each policy and procedure of the security-based swap dealer or major security-based swap participant of the chief compliance officer (including the code of ethics and conflict of interest policies).
- (B) REQUIREMENTS.—A compliance report under subparagraph (A) shall—
- (i) accompany each appropriate financial report of the security-based swap dealer or major security-based swap participant that is required to be furnished to the Commission pursuant to this section; and
 - (ii) include a certification that, under penalty of law, the compliance report is accurate and complete.
- (1) ENFORCEMENT AND ADMINISTRATIVE PROCEEDING AUTHORITY.—
- (1) PRIMARY ENFORCEMENT AUTHORITY.—
- (A) SECURITIES AND EXCHANGE COMMISSION.—Except as provided in subparagraph (B), (C), or (D), the Commission shall have primary authority to enforce subtitle B, and the amendments made by subtitle B of the Wall Street Transparency and Accountability Act of 2010, with respect to any person.
- (B) PRUDENTIAL REGULATORS.—The prudential regulators shall have exclusive authority to enforce the provisions of subsection (e) and other prudential requirements of this title (including risk management standards), with respect to security-based swap dealers or major security-based swap participants for which they are the prudential regulator.
- (C) REFERRAL.—
- (i) VIOLATIONS OF NONPRUDENTIAL REQUIREMENTS.—If the appropriate Federal banking agency for security-based swap dealers or major security-based swap participants that are depository institutions has cause to believe that such security-based swap dealer or major security-based swap participant may have engaged in conduct that constitutes a violation of the

nonprudential requirements of this section or rules adopted by the Commission thereunder, the agency may recommend in writing to the Commission that the Commission initiate an enforcement proceeding as authorized under this title. The recommendation shall be accompanied by a written explanation of the concerns giving rise to the recommendation.

(ii) VIOLATIONS OF PRUDENTIAL REQUIREMENTS.—If the Commission has cause to believe that a securities-based swap dealer or major securities-based swap participant that has a prudential regulator may have engaged in conduct that constitute a violation of the prudential requirements of subsection (e) or rules adopted thereunder, the Commission may recommend in writing to the prudential regulator that the prudential regulator initiate an enforcement proceeding as authorized under this title. The recommendation shall be accompanied by a written explanation of the concerns giving rise to the recommendation.

(D) BACKSTOP ENFORCEMENT AUTHORITY.—

(i) INITIATION OF ENFORCEMENT PROCEEDING BY PRUDENTIAL REGULATOR.—If the Commission does not initiate an enforcement proceeding before the end of the 90-day period beginning on the date on which the Commission receives a written report under subsection (C)(i), the prudential regulator may initiate an enforcement proceeding.

(ii) INITIATION OF ENFORCEMENT PROCEEDING BY COMMISSION.—If the prudential regulator does not initiate an enforcement proceeding before the end of the 90-day period beginning on the date on which the prudential regulator receives a written report under subsection (C)(ii), the Commission may initiate an enforcement proceeding.

(2) CENSURE, DENIAL, SUSPENSION; NOTICE AND HEARING.—The Commission, by order, shall censure, place limitations on the activities, functions, or operations of, or revoke the registration of any security-based swap dealer or major security-based swap participant that has registered with the Commission pursuant to subsection (b) if the Commission finds, on the record after notice and opportunity for hearing, that such censure, placing of limitations, or revocation is in the public interest and that such security-based swap dealer or major security-based swap participant, or any person associated with such security-based swap dealer or major security-based swap participant effecting or involved in effecting transactions in security-based swaps on behalf of such security-based swap dealer or major security-based swap participant, whether prior or subsequent to becoming so associated—

(A) has committed or omitted any act, or is subject to an order or finding, enumerated in subparagraph (A), (D), or (E) of paragraph (4) of section 15(b);

(B) has been convicted of any offense specified in subparagraph (B) of such paragraph (4) within 10 years of the commencement of the proceedings under this subsection;

(C) is enjoined from any action, conduct, or practice specified in subparagraph (C) of such paragraph (4);

(D) is subject to an order or a final order specified in subparagraph (F) or (H), respectively, of such paragraph (4); or

(E) has been found by a foreign financial regulatory authority to have committed or omitted any act, or violated any foreign statute or regulation, enumerated in subparagraph (G) of such paragraph (4).

(3) ASSOCIATED PERSONS.—With respect to any person who is associated, who is seeking to become associated, or, at the time of the alleged misconduct, who was associated or was seeking to become associated with a security-based swap dealer or major security-based swap participant for the purpose of effecting or being involved in effecting security-based swaps on behalf of such security-based swap dealer or major security-based swap participant, the Commission, by order, shall censure, place limitations on the activities or functions of such person, or suspend for a period not exceeding 12 months, or bar such person from being associated with a security-based swap dealer or major security-based swap participant, if the Commission finds, on the record after notice and opportunity for a hearing, that such censure, placing of limitations, suspension, or bar is in the public interest and that such person—

(A) has committed or omitted any act, or is subject to an order or finding, enumerated in subparagraph (A), (D), or (E) of paragraph (4) of section 15(b);

(B) has been convicted of any offense specified in subparagraph (B) of such paragraph (4) within 10 years of the commencement of the proceedings under this subsection;

(C) is enjoined from any action, conduct, or practice specified in subparagraph (C) of such paragraph (4);

(D) is subject to an order or a final order specified in subparagraph (F) or (H), respectively, of such paragraph (4); or

(E) has been found by a foreign financial regulatory authority to have committed or omitted any act, or violated any foreign statute or regulation, enumerated in subparagraph (G) of such paragraph (4).

(4) UNLAWFUL CONDUCT.—It shall be unlawful—

(A) for any person as to whom an order under paragraph (3) is in effect, without the consent of the Commission, willfully to become, or to be, associated with a security-based swap dealer or major security-based swap participant in contravention of such order; or

(B) for any security-based swap dealer or major security-based swap participant to permit such a person, without the consent of the Commission, to become or remain a person associated with the security-based swap dealer or major security-based swap participant in contravention of such order, if such security-based swap dealer or major se-

curity-based swap participant knew, or in the exercise of reasonable care should have known, of such order.

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