

# **PAPERWORK REDUCTION ACT SUBMISSION**

## **Rules 17Ad-22**

### **Supporting Statement**

#### **A. JUSTIFICATION**

##### **1. Necessity of Information Collection**

###### **Legal and Administrative Requirements**

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

Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank Act”) added new provisions to the Securities Exchange Act of 1934 (“Exchange Act”) that require clearing agencies that clear security-based swaps (“security-based swap clearing agencies”) to register with the Securities Exchange Commission (“Commission”) and require the Commission to adopt rules with respect to security-based swap clearing agencies.

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

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

Title VIII of the Dodd-Frank Act, entitled the Payment, Clearing, and Settlement Supervision Act of 2010 (“Clearing Supervision Act”), establishes an enhanced supervisory and risk control system for systemically important clearing agencies and other financial market utilities (“FMUs”). It provides that the Commission may prescribe regulations containing risk management standards, taking into consideration relevant international standards and existing prudential requirements, for any designated clearing entities it regulates. While no designations have been made with respect to whether any FMU is, or is likely to become, systemically important, the Commission believes it is beneficial to consider the requirements of the Clearing Supervision Act in its rules for clearing agencies because the Clearing Supervision Act may apply to one or more clearing agencies in the future and the Commission preliminarily believes that its goals are consistent with the goals of Section 17A of the Exchange Act. Specifically, Congress recognized in the Clearing Supervision Act that the operation of multilateral payment, clearing or settlement activities may reduce risks for clearing participants and the broader financial system, while at the same time creating new risks that require multilateral payment, clearing or settlement activities to be well-designed and operated in a safe and sound manner. The Clearing Supervision Act is designed, in part, to provide a regulatory framework to help deal with such risk management issues, which is generally consistent with the Exchange Act

requirement that clearing agencies be organized in a manner so as to facilitate prompt and accurate clearance and settlement, safeguard securities and funds and protect investors.

### iii. Section 17A of Exchange Act

As noted above, in addition to the new authority provided to the Commission under Titles VII and VIII of the Dodd-Frank Act, the Commission has existing authority over clearing agencies under the Exchange Act. For example, entities are required to register with the Commission pursuant to Section 17A of the Exchange Act and Rule 17Ab2-1, prior to performing the functions of a clearing agency. Under this registration system, the Commission is not permitted to grant registration unless it determines that the rules and operations of the clearing agency meet the standards set forth in Section 17A. Specifically, Sections 17A(b)(3)(A)-(I) identify determinations that the Commission must make about the rules and structure of a clearing agency prior to granting registration. If a clearing agency is granted registration, the Commission oversees the clearing agency to facilitate compliance with the Exchange Act through the rule filing process for self-regulatory organizations (“SROs”) and through on-site examinations by Commission staff. Section 17A also gives the Commission authority to adopt rules for clearing agencies as necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Exchange Act and prohibits a registered clearing agency from engaging in any activity in contravention of these rules and regulations.

### **Rules Governing Clearing Agencies<sup>1</sup>**

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

For a clearing agency to be registered under Section 17A of the Exchange Act, it must have the ability to facilitate the prompt and accurate clearance and settlement of transactions, safeguard investor funds and securities, remove impediments to and perfect the mechanism of a national clearance and settlement system, and to generally protect investors. Also, the clearing agency’s rules must provide adequate access to qualified participants, fair representation of shareholders and participants, equitable pricing, fair discipline of participants, and must not impose any undue burden on competition. The Commission is adopting Rule 17Ad-22 (“Rule”) to require clearing agencies to establish, implement, maintain and enforce written policies and procedures designed to promote effective risk management procedures and controls as well as meet the statutory requirements under the Exchange Act on an ongoing basis.

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<sup>1</sup> See infra Section 15 regarding discussion of key differences between the Adopting Release and the Proposing Release.

The establishment of consistent standards for clearing agencies that offer central counterparty (“CCP”) and central securities depository (“CSD”) services is an important goal that underpinned the enactment of Section 17A of the Exchange Act. Rule 17Ad-22 establishes minimum standards for the operations and risk management practices for clearing agencies that are consistent with the standards for CCPs and CSDs operating domestically and in other jurisdictions. At this time, the Commission does not intend for Rule 17Ad-22 to apply to clearing agencies that perform post-trade processing services (i.e., comparison of trade data, collateral management and tear-up/compression). The scope of Rule 17Ad-22 will be limited to clearing agencies that are registered with the Commission and the rule will not apply to any clearing agencies operating pursuant to an exemption from registration as a clearing agency granted by the Commission, unless the terms of future exemptions specifically contemplate its application, in whole or in part. The Commission has clarified this as part of the final Rule 17Ad-22 by adding the word “registered” before the term “clearing agency” appearing in the first instance in paragraphs (b), (c)(1), (c)(2), and (d). For this reason, references to the term “clearing agency” in the Adopting Release are generally intended to capture only registered clearing agencies, unless the context suggests otherwise. The Commission may consider at a later time whether rules tailored to clearing agencies that provide post-trade processing services would be appropriate.

There are a number of collections of information contained in the Rule. The information collected in these provisions is necessary to carry out the mandates of the Exchange Act, as amended by the Dodd-Frank Act.

The statutory basis for the Rule is as follows: Exchange Act Section 3C, 15 U.S.C. 78c-3; Exchange Act Section 17A, 15 U.S.C. 78q-1; and 12 U.S.C. 5464(a)(2).

## **2. Purpose and Use of the Information Collection**

### **i. Standards for Clearing Agencies**

#### **a. Measurement and Management of Credit Exposures**

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

#### **b. Margin Requirements**

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

c. Financial Resources

Rule 17Ad-22(b)(3) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to maintain sufficient financial resources to withstand, at a minimum, a default by the participant family to which it has the largest exposure in extreme but plausible market conditions, provided that a registered clearing agency acting as a central counterparty for security-based swaps shall maintain additional financial resources sufficient to withstand, at a minimum, a default by the two participant families to which it has the largest exposures in extreme but plausible market conditions, in its capacity as a central counterparty for security-based swaps. The purpose of the collection of information is to enable the clearing agency to satisfy all of its settlement obligations in the event of a participant default.

d. Model Validation

Rule 17Ad-22(b)(4) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed to provide for an annual model validation consisting of evaluating the performance of the clearing agency's margin models and the related parameters and assumptions associated with such models by a qualified person who is free from influence from the persons responsible for the development or operation of the models being validated. The purpose of the collection of information is to enable the clearing agency to obtain an assessment of its margin model by a qualified, independent person.

e. Non-Dealer Access

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

f. Portfolio Size and Transaction Volume Restrictions

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

g. Net Capital Restrictions

Rule 17Ad-22(b)(7) would require a clearing agency that provides CCP services to establish, implement, maintain and enforce written policies and procedures reasonably designed

to provide a person that maintains net capital equal to or greater than \$50 million with the ability to obtain membership at the clearing agency, provided that such persons are able to comply with other reasonable membership standards, with any net capital requirements being scalable so that they are proportional to the risks posed by the participant's activities to the clearing agency. The rule also permits a clearing agency to provide for a higher net capital requirement (i.e., higher than \$50 million) as a condition for membership at the clearing agency if the clearing agency demonstrates to the Commission that such a requirement is necessary to mitigate risks that could not otherwise be effectively managed by other measures, such as scalable limitations on the transactions that the participants may clear through the clearing agency, and the Commission approves the higher net capital requirement as part of a rule filing or clearing agency registration application. The purpose of the collection of information is to remove unnecessary barriers to clearing access by market participants with a net capital level above \$50 million, while at the same time facilitating sound risk management practices by clearing agencies by encouraging them to examine and articulate the benefits that higher net capital requirements would create through having clearing agencies develop scalable membership standards that links the activities any participants could potentially engage in with the potential risks posed by the participant.

h. Record of Financial Resources

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

i. Annual Audited Financial Statements

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

j. Transparent and Enforceable Rules and Procedures

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

k. Participation Requirements

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

l. Custody of Assets and Investment Risk

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

m. Identification and Mitigation of Operational Risk

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

n. Money Settlement Risks

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

o. Cost-Effectiveness

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

p. Links

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

q. Governance

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

r. Information on Services

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

appropriate actions to mitigate their risks and costs associated with the use of the clearing agency.

s. Immobilization and Dematerialization of Stock Certificates

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

t. Default Procedures

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

u. Timing of Settlement Finality

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

v. Delivery Versus Payment

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

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

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



enable clearing agencies to satisfy their settlement obligations on time and for the agreed upon terms.

x. **Identification and Management of Physical Delivery Risks**

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

**3. Consideration of Information Technology**

The Rule is drafted to utilize as much information technology as possible in collecting the information. Over time, the Commission expects that the burden will be reduced due to future technology enhancements. The Commission is not aware of any technical or legal obstacles to reducing the burden through the use of improved information technology.

**4. Duplication**

Section 712(a)(2) of the Dodd-Frank Act provides that, before commencing any rulemaking regarding, among other things, clearing agencies with regard to security-based swaps, the Commission must consult and coordinate with the Commodity Futures Trading Commission ("CFTC") and other prudential regulators for the purposes of assuring regulatory consistency and comparability, to the extent possible. The Commission staff and the CFTC staff have consulted and coordinated with one another regarding their respective Commissions' rules regarding clearing agencies as mandated by the Dodd-Frank Act. The Commission staff has also consulted and coordinated with other prudential regulators. The Rule does not duplicate information required to be collected elsewhere.

**5. Effect on Small Entities**

The Rule would not affect any small entities.

**6. Consequences of Not Conducting Collection**

The Dodd-Frank Act enacted sweeping reforms in the financial system, including FMUs such as clearing agencies. It also charged the Commission with significant duties in carrying out these reforms. The consequences of not conducting collections of information or any less frequent collections of information pursuant to the Rule would significantly impair the Commission's ability to carry out its statutory obligations under the Exchange Act, as amended by Titles VII and VIII of the Dodd-Frank Act.

## **7. Inconsistencies with Guidelines in 5 CFR 1320.8(d)**

The information collection is consistent with the general information collection guidelines imposed for public protection as set forth in 5 CFR 1320.5(d)(2),

## **8. Consultations Outside the Agency**

The Commission has issued a release soliciting comment on the new “collection of information” requirements and associated paperwork burdens.<sup>2</sup> Comments were due by April 29, 2011. The Commission received 25 comment letters. Comments were generally received from registrants, investors, and other market participants. In addition, the Commission and staff participate in ongoing dialogue with representatives of various market participants through public conferences, meetings and informal exchanges. The Commission considered all comments received prior to publishing the final rule, and explains in the Adopting Release how the final rule responds to such comments, in accordance with 5 C.F.R. 1320.11(f). The comments received on the proposed rulemaking and are posted on the Commission’s public website, and are available through <http://www.sec.gov/rules/proposed.shtml>.

Some commenters expressed general concerns about the burden of regulation, but such comments focused on rules in the Proposing Release not being adopted today and on areas that go beyond the scope of the Adopting Release.<sup>3</sup> Commenters expressed concerns about the burdens associated with parts of Rule 17Ad-22(b), and those comments are addressed below. Commenters did not specifically comment on the burdens associated with Rule 17Ad-22(c)–(d). To the extent that commenters submitted comments about the costs of implementing the proposed rules or requested changes in proposed rules, those comments are also set out below.

### Proposed Rules Generally

- One commenter noted that complex clearing organizations have many subsidiaries that engage in many different activities and are subject to regulation by many different regulators. Such organizations need the flexibility, to the extent possible, to structure their enterprise-wide programs in a way that works with each business and complies with all applicable laws and regulations.
  - The commenter argued that is particularly the case with respect to compliance programs because if the proposed rules are overly prescriptive, organizations such as

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<sup>2</sup> See Exchange Act Release No. 34-64017 (Mar. 3, 2011), 76 FR 14472 (Mar. 16, 2011) (“Proposing Release”), available at <http://www.sec.gov/rules/proposed/2011/34-64017fr.pdf>.

<sup>3</sup> See, e.g., ICE Letter at 1-2 (stating that “[p]ost-trade processing service providers would be unable to distribute end-of-day settlement prices, as required by the Proposal, and the record keeping requirements of the Proposal would prove so burdensome to such providers that the efficiency and alacrity that they provide to the CDS industry would be adversely affected.”).

DTCC may be subject to conflicting requirements and may be forced to fragment certain enterprise-wide programs to comply with such conflicting requirements, which could substantially increase costs and compliance risks within such organizations.

➤ Further, if the proposed rules are overly prescriptive, they may prevent clearing agencies from being able to adapt quickly to changes in markets and global standards and that retaining that flexibility is extremely important.<sup>4</sup>

➤ The commenter noted that many of the proposed rules require a clearing agency to establish, implement, maintain and enforce written policies and procedures and stated its belief that the precise form of these written policies and procedures should be a matter for the clearing agency to determine (so long as they are compliant) and may include service guides, operational arrangements, compliance procedures, link and cross-guaranty agreements and materials relating to internal operations and controls.<sup>5</sup>

- Another commenter requested that if the rules are adopted as proposed then the rules should not become effective until at least two years after their approval and that at a minimum compliance with any "two largest participants" standard that the SEC might adopt in proposed Rule 17Ad-22(b)(3) should be subject to a two year delayed implementation schedule.<sup>6</sup>
- The commenter stated that if the rules are adopted as proposed it will require extensive new policies and procedures, drafting, proposing and obtaining approval of necessary rules and rule changes, executing plans to raise additional financial resources conducting extensive internal training, hiring of additional compliance personnel and many other tasks while also taking many other steps to comply with other aspects of the Dodd-Frank Act.<sup>7</sup>
- The commenter also noted that phase in periods would be appropriate because the rules would require that clearing agencies :
  - review their existing policies and procedures for compliance with the proposed rules;
  - develop and draft new policies and procedures to implement new requirements of the proposed rules;
  - prepare and obtain Commission approval for rule changes under Section 19(b) of the Exchange Act; and
  - in all likelihood, hire and train additional personnel.

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<sup>4</sup> See letter from Larry E. Thompson, General Counsel, The Depository Trust & Clearing Corporation, dated April 29, 2011 ("The DTCC (April) Letter") at 6-7.

<sup>5</sup> See The DTCC (April) Letter at 7.

<sup>6</sup> See letter from William H. Navin, Executive Vice President, General Counsel, and Secretary, The Options Clearing Corporation, dated April 29, 2011 ("The OCC Letter") at 17.

<sup>7</sup> See The OCC Letter at 17.

A number of the proposed rules impose new operational requirements on clearing agencies that may require very significant changes in their operational arrangements.<sup>8</sup>

- One commenter strongly encouraged the SEC to avoid final action on its proposed rules before it has greater clarity on what clearinghouse regulations are ultimately adopted by European and U.K. regulators and what approaches to regulation are embraced by CPSS-IOSCO. This would allow the SEC to adopt rules that would not unknowingly force market activity into other jurisdictions by virtue of associated regulatory costs.<sup>9</sup>

#### Rule 17Ad-22

- One commenter supported the rule with certain clarifications and stated that proposed Rule 17Ad-22(b)(4) is overly prescriptive in two respects.<sup>10</sup>
  - First, the commenter expressed that the rule should not require the validation to be performed on an annual basis. Instead, the frequency should be left to the discretion of the clearing agency because it is in the best position to determine the appropriate timing.<sup>11</sup>
    - The commenter supported its contention that the proposed rule is overly prescriptive by stating that the requirement for an annual validation is unnecessary and may be overly burdensome in the absence of a material change in the model or a material change in the market environment that may affect the model.<sup>12</sup>
  - Second, the commenter argued that the clearing agency performing central counterparty services is in the best position to determine how to achieve the goal of performing a candid assessment that is free from outside influences and therefore the rule should not prescribe a particular method of achieving that outcome.<sup>13</sup>
    - The commenter pointed out that with respect to achieving independence in a model validation review the Board of Governors of the Federal Reserve System and the Office of the Comptroller of the Currency stated in the recent Supervisory Guidance on Model Risk Management that independence "may be supported by separation of reporting lines" but that it "should be judged by

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<sup>8</sup> See The DTCC (April) Letter at 6.

<sup>9</sup> See The OCC Letter at 3.

<sup>10</sup> See The DTCC (April) Letter at 13.

<sup>11</sup> See The DTCC (April) at Letter 13.

<sup>12</sup> See The DTCC (April) Letter at 13.

<sup>13</sup> See The DTCC (April) Letter at 13.

actions and outcomes, since there may be additional ways to ensure objectivity and prevent bias.”<sup>14</sup>

- The commenter recommends that the SEC replace the aspect of the currently proposed rule text that addresses independence with the language already in the corresponding discussion section of the release, which states that "the person validating the clearing agency's model should be sufficiently free from outside influences so that he or she can be completely candid in their assessment of the model.”<sup>15</sup>
- In sum, the commenter recommended that the 17Ad-22(b)(4) rule text be recast as follows: "(b) A clearing agency that performs central counterparty services shall establish, implement, maintain and enforce written policies and procedures reasonably designed to: (4) Provide for periodic model validation consisting of evaluating the performance of the clearing agency's margin models and the related parameters and assumptions associated with such models by a qualified person who is sufficiently free from outside influences to perform a candid evaluation of such models."
  - The commenter did not believe that any additional changes are necessary to rule 17Ad-22(b)(4) and stated its belief that this approach is more consistent with Recommendation 4 from the CPSS-IOSCO Recommendations for Central Counterparties and with Principles for Financial Market Infrastructures Principle 6 because it does not prescribe a model validation frequency or a specific way to ensure the integrity of the validation process.<sup>16</sup>
- One commenter expressed that proposed Rules 17Ad-22(b)(5)–(7) providing for mandatory access to CCPs in certain circumstances goes “beyond anything in current or proposed global standards. . . [and is, therefore,] unnecessary and counterproductive to the goal of fair and open access within a framework of safe and sound operation.”<sup>17</sup>
- One commenter responded to the challenges of bringing independence to the model review process by explaining that if it undertook to detach model review entirely from model development it would be necessary to have two quantitative teams which presents the following issues:
  - Cost of staff;

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<sup>14</sup> See The DTCC (April) Letter at 14.

<sup>15</sup> See The DTCC (April) Letter at 14.

<sup>16</sup> See The DTCC (April) Letter at 15.

<sup>17</sup> See The DTCC (April) Letter at 5; see also The DTCC (April) Letter at 4 (stating that “[t]he application of global standards to clearing agencies will also prevent clearing agencies and their participants from incurring unnecessary expense associated with complying with different, and potentially conflicting regulatory standards.”).

- Staffing problems since talented young people with the requisite quantitative skills tend to see review as non-creative;
  - Adversarial relations (a team dedicated solely to review may be seen to contribute only if it finds fault; and
  - Tensions that require senior management to resolve highly technical disputes between the development and review teams.<sup>18</sup>
- Regarding proposed Rule 17Ad-22(d)(8), one commenter urged the SEC not to adopt hard and fast standards that will be costly to implement and maintain and that yield little or no apparent corresponding regulatory benefits.<sup>19</sup>
- One commenter expressed concern that proposed Rule 17Ad-22(d)(12) could be interpreted to provide intraday or real-time finality beyond what clearing agencies currently provide and beyond what they can provide without devoting resources to make significant changes in systems and processes.<sup>20</sup>
    - Therefore, the commenter suggested that the Commission should make clear in the final rule that the rule is not intended to impose an obligation on clearing agencies to provide intraday or real-time finality beyond what they currently provide or any obligation to build such additional capability unless and until there is industry and regulatory consensus on whether and what additional capability to build and how to allocate the cost.<sup>21</sup>

## 9. **Payment or Gift**

Not applicable.

## 10. **Confidentiality**

### i. **Standards for Clearing Agencies**

#### a. **Measurement and Management of Credit Exposures**

The collection of information relating to the measurement and management of credit exposures under Rule 17Ad-22(b)(1) would not require disclosure of information to the Commission staff.

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<sup>18</sup> See The OCC Letter at 11.

<sup>19</sup> See letter from Craig S. Donohue, CME Group, dated April 29, 2011 (“CME Letter”) at 4.

<sup>20</sup> See The DTCC (April) Letter at 25.

<sup>21</sup> See The DTCC (April) Letter at 25.

b. Margin Requirements

The collection of information relating to margin requirements under Rule 17Ad-22(b)(2) would not require disclosure of information to the Commission staff.

c. Financial Resources

The collection of information relating to financial resources under Rule 17Ad-22(b)(3) would not require disclosure of information to the Commission staff.

d. Model Validation

The collection of information relating to conducting an annual model validation under Rule 17Ad-22(b)(4) would not require disclosure of information to the Commission staff.

e. Non-Dealer Access

The collection of information relating to non-dealer access under Rule 17Ad-22(b)(5) would not require disclosure of information to the Commission staff.

f. Net Capital Requirements

The collection of information relating to the procedures for net capital requirements under Rule 17Ad-22(b)(7) would not require disclosure of information to the Commission staff.

g. Record of Financial Resources

The collection of information relating to the calculation and maintenance by a clearing agency that provides CCP services of a quarterly report describing the financial resources necessary to meet the requirements of Rule 17Ad-22(b)(3) would not require disclosure of information to the Commission staff.

h. Annual Audited Financial Statements

The collection of information relating to the annual audited financial statements published to the clearing agency's website under Rule 17Ad-22(c)(2) would be subject to public availability.

i. Transparent and Enforceable Rules and Procedures

The collection of information relating to a clearing agency's well-founded, transparent and enforceable legal framework under Rule 17Ad-22(d)(1) would not require disclosure of information to the Commission staff.

j. Participation Requirements

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

k. Custody of Assets and Investment Risk

The collection of information relating to minimizing custody and investment risk under Rule 17Ad-22(d)(3) would not require disclosure of information to the Commission staff.

l. Identification and Mitigation of Operational Risk

The collection of information relating to identifying and minimizing operational risk under Rule 17Ad-22(d)(4) would not require disclosure of information to the Commission staff.

m. Money Settlement Risks

The collection of information relating to the procedures for money settlement arrangements under Rule 17Ad-22(d)(5) would not require disclosure of information to the Commission staff.

n. Cost-Effectiveness

The collection of information relating to being cost-effectiveness under Rule 17Ad-22(d)(6) would not require disclosure of information to the Commission staff.

o. Links

The collection of information relating to evaluating potential sources of risk in links arrangements under Rule 17Ad-22(d)(7) would not require disclosure of information to the Commission staff.

p. Governance

The collection of information relating to a clearing agency's governance arrangements under Rule 17Ad-22(d)(8) would not require disclosure of information to the Commission staff.

q. Information on Services

The collection of information relating to the provision of sufficient information to market participants under Rule 17Ad-22(d)(9) would not require disclosure of information to the Commission staff.



r. Immobilization and Dematerialization of Stock Certificates

The collection of information relating to the procedures for immobilizing and dematerializing stock certificates under Rule 17Ad-22(d)(10) would not require disclosure of information to the Commission staff.

s. Default Procedures

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

t. Risk Controls to Address Participants' Failure to Settle

The collection of information relating to risk controls to address participants' failure to settle under Rule 17Ad-22(d)(14) would not require disclosure of information to the Commission staff.

u. Identification and Management of Physical Delivery Risks

The collection of information relating to the statement and management of physical delivery risk under Rule 17Ad-22(d)(15) would not require disclosure of information to the Commission staff.

**11. Sensitive Questions**

Not applicable. There are no questions of a sensitive nature asked.

**12. Burden of Information Collection**

Rules 17Ad-22(b)(1)–(3) and Rules 17Ad-22(d)(1)–(15) are discussed together because these rules represent usual and customary practices already being implemented by registered clearing agencies. Because Rules 17Ad-22(b)(4), (b)(5)–(7) and (c), respectively establish new minimum practices for registered clearing agencies with regard to model validation, membership practices and certain financial information, the Adopting Release discusses these rules separately.

i. Number of Respondents

Standards in Rules 17Ad-22(b)(1)-(3) and (d)(1)-(15) that Impose a PRA Burden

The Commission believes that the standards in Rule 17Ad-22(b)(1)-(3) and (d)(1)-(15) impose a PRA burden. As noted above, registered clearing agencies already have written policies and procedures that meet the standards set forth in Rules 17Ad-22(b)(1)–(3) and (d)(1)–(15) as part of their usual and customary business practice. Accordingly, the Commission believes that the registered clearing agencies would not need to build new infrastructure or modify operations to continue to meet Rule 17Ad-22(b)(1)–(3) and (d)(1)–(15). The Commission believes that registered clearing agencies will incur the incremental burdens of

reviewing existing policies and procedures for compliance and updating existing policies and procedures where appropriate. Thus, for these provisions, the Commission estimates that there would be ten respondent clearing agencies.

#### Standards in Rule 17Ad-22(b)(4) that Impose a PRA Burden

The requirement to develop written policies and procedures in Rule 17Ad-22(b)(4) imposes a PRA burden. The requirement in Rule 17Ad-22(b)(4) will apply to all CCPs. As discussed above, the Commission estimates that nine CCPs will be subject to the burdens under Rule 17Ad-22(b)(4).

#### Standards in Rules 17Ad-22(b)(5)-(7) that Impose a PRA Burden

The requirements to develop written policies and procedures in Rules 17Ad-22(b)(5)–(7) impose a PRA burden. These PRA burdens will apply to all CCPs. As discussed above, the Commission estimates that nine CCPs will be subject to the burdens under Rules 17Ad-22(b)(5)–(7). The Commission believes that CCPs are more likely to be able to address the changes required by Rules 17Ad-22(b)(5)–(7) in an integrated, not piecemeal, review and drafting process to implement policies and procedures responsive to these rules. Therefore, the revised PRA burden estimates no longer account for each requirement as a separate burden.

#### Standards in Rule 17Ad-22(c) that Impose a PRA Burden

The standards in Rule 17Ad-22(c) impose a PRA burden.<sup>22</sup> The requirements of Rule 17Ad-22(c) will apply to all registered clearing agencies (ten respondent clearing agencies).

#### Standards in Rule 17Ad-22(c)(1) that Impose a PRA Burden

The standards in Rule 17Ad-22(c)(1) impose a PRA burden. The requirements of Rule 17Ad-22(c)(1) will apply to CCPs (nine respondent CCPs).

#### Standards in Rule 17Ad-22(c)(2) that Impose a PRA Burden

The standards in Rule 17Ad-22(c)(2) impose a PRA burden. The requirements of Rule 17Ad-22(c)(2) will apply to all registered clearing agencies (ten respondent clearing agencies).

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<sup>22</sup> The burden discussion for the different information collection requirements of Rule 17Ad-22(c)(1)–(2) has been split into sections to account for the different requirements for varying numbers of respondents. Rule 17Ad-22(c) imposes an overall burden relating to policies and procedures and system adjustments on all registered clearing agencies, while Rule 17Ad-22(c)(1), as discussed below, imposes on CCPs an ongoing burden to generate the required reports concerning their financial resources and Rule 17Ad-22(c)(2), as discussed below, imposes initial and ongoing burdens related to annual audited financial statements to all registered clearing agencies, some of which are already implementing this requirement as part of their usual and customary practices.

ii. Source of Estimates, Annual Hour Burden, and Explanation of Estimates

Standards in Rules 17Ad-22(b)(1)–(3) and (d)(1)–(15) that Impose a PRA Burden

The requirements to develop written policies and procedures in Rules 17Ad-22(b)(1)–(3) and Rules 17Ad-22(d)(1)–(15) impose a recordkeeping PRA burden. The requirements in Rules 17Ad-22(b)(1)–(3) will apply to CCPs that are registered clearing agencies. The Commission estimates that a total of nine CCPs<sup>23</sup> will be subject to the burdens under Rules 17Ad-22(b)(1)–(3). Currently, six clearing agencies are registered to provide CCP services, and the Commission estimates that three more entities could register as clearing agencies to provide CCP services. The requirements in Rules 17Ad-22(d)(1)–(15) (with the exception of Rules 17Ad-22(d)(10) and (13)–(15), which are applicable only to CSDs), on the other hand, apply to all registered clearing agencies, of which there could potentially be a total of ten entities, including the one registered clearing agency that is a CSD.

As noted above, registered clearing agencies already have written policies and procedures that meet the standards set forth in Rules 17Ad-22(b)(1)–(3) and (d)(1)–(15) as part of their usual and customary business practice. Accordingly, the Commission believes that the registered clearing agencies would not need to build new infrastructure or modify operations to continue to meet Rule 17Ad-22(b)(1)–(3) and (d)(1)–(15). The Commission believes that registered clearing agencies will incur the incremental burdens of reviewing existing policies and procedures for compliance and updating existing policies and procedures where appropriate. The requirements would impose an aggregate one-time burden of approximately 1,750 hours for all registered clearing agencies.<sup>24</sup> The standards contained in Rule 17Ad-22(d) would also impose ongoing burdens on registered clearing agencies. For example, Rules 17Ad-22(b)(1)–(3) and (d)(1)–(15) would require registered clearing agencies to perform certain ongoing monitoring and enforcement activities with respect to the written policies and procedures the registered clearing agency creates in response to the standard. Accordingly, after the first year, the Commission believes that those ongoing activities would impose an aggregate annual burden of approximately 600 hours for all respondent clearing agencies.<sup>25</sup> Because recent assessments of the registered U.S. clearing agencies support the conclusion that clearing agencies and their rule

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<sup>23</sup> The Commission believes that there is a potential for new security-based swap clearing agencies to form but does not expect there to be a large number based on the significant level of capital and other financial resources needed for the formation of a clearing agency.

<sup>24</sup> This figure was calculated as follows: ((Assistant General Counsel at 60 hours) + (Compliance Attorney at 85 hours) + (Computer Operations Manager at 15 hours) + (Senior Business Analyst at 15 hours)) = 175 hours x 10 respondent clearing agencies = 1,750 hours.

<sup>25</sup> This figure was calculated as follows: Compliance Attorney at 60 hours x 10 respondent clearing agencies = 600 hours.

For each respondent clearing agency, the estimated annualized burden for Rules 17Ad-22(b)(1)–(3) and (d)(1)–(15) is 98 hours (figure calculated as follows: 175 hours (Year 1 burden) + 60 hours (Year 2 burden) + 60 hours (Year 3 burden) = 295 hours (estimated total burden over 3 years) ÷ 3 years = 98 hours).

books generally meet or exceed analogous standards of operation and governance to those standards within Rules 17Ad-22(b)(1)–(3) and (d)(1)–(15),<sup>26</sup> the Commission believes that the burden estimate for the aggregate one-time burden should be revised down from the burden estimated in the Proposing Release. The Commission estimates that because these initial compliance efforts will largely comprise a review of existing policies and procedures, the aggregate one-time burden on respondent clearing agencies will be incremental to their current compliance processes. The expected review of current policies and procedures will likely not involve much involvement by the information technology staff at the clearing agency or much involvement by the clearing agency’s assistant general counsel because the requirements of these rules have already been written into and have been implemented as part of the policies and procedures of registered clearing agencies. Accordingly, those burden estimates have been reduced and the burden estimate for the compliance attorney, who will most likely perform most of the review of current policies and procedures, has been increased. In order to estimate the one-time burden and annual burden for ongoing activities, we looked to the burdens imposed by similar policies and procedures requirements in Regulation NMS as a guide and adapted those figures for the purposes of this release.<sup>27</sup>

#### Standards in Rule 17Ad-22(b)(4) that Impose a PRA Burden

The requirement to develop written policies and procedures in Rule 17Ad-22(b)(4) imposes a recordkeeping PRA burden. The requirement in Rule 17Ad-22(b)(4) will apply to all CCPs. The Commission estimates that nine CCPs will be subject to the burdens under Rule 17Ad-22(b)(4).

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS, the Commission has preserved the burden estimates from the Proposing Release. The Commission estimates that Rule 17Ad-22(b)(4) would impose a one-time burden on each respondent CCP of 210 hours, corresponding to an aggregate one-time burden on all respondent CCPs of 1,890 hours.<sup>28</sup>

Rule 17Ad-22(b)(4) would require one-time systems adjustments related to the capability to perform an annual model validation. These adjustments would amount to a one-time systems adjustment burden per respondent of 100 hours, or an aggregate one-time burden of approximately 900 hours.<sup>29</sup> Taking into account the afore-mentioned policies and procedures one-time burden, the total one-time burden per respondent for this rule is 310 hours.

<sup>26</sup> See Proposing Release, supra note 2, at 14509.

<sup>27</sup> See Exchange Act Release Nos. 51808 (June 9, 2005), 70 FR 37496 (June 29, 2005) (discussing in Section VIII.A.4 the time needed from legal, compliance, information technology and business operations personnel to create policies and procedures for preventing and monitoring trade-throughs).

<sup>28</sup> This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours x 9 respondent CCPs = 1,890 hours.

<sup>29</sup> This figure was calculated as follows: ((Chief Compliance Officer for 40 hours) + (Computer Department Operations Manager for 40 hours) + (Senior Programmer for 20 hours)) = 100 hours x 9 respondent CCPs = 900 hours.

CCPs would be required to collect information relating to their model validation standards required by Rule 17Ad-22(b)(4) on an ongoing basis. The Commission expects that the exact burden of administering the procedures for model validation standards would vary depending on how frequently each CCP may need to update its procedures. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS, the Commission estimates that the ongoing requirements of this rule after the first year would impose an annual burden of 60 hours on each respondent CCP, corresponding to an aggregate annual burden for all respondent CCPs of 540 hours.<sup>30</sup>

#### Standards in Rules 17Ad-22(b)(5)–(7) that Impose a PRA Burden

The requirements to develop written policies and procedures in Rules 17Ad-22(b)(5)–(7) impose a recordkeeping PRA burden. These PRA burdens will apply to all CCPs. The Commission estimates that nine CCPs will be subject to the burdens under Rules 17Ad-22(b)(5)–(7). The Commission believes that CCPs are more likely to be able to address the changes required by Rules 17Ad-22(b)(5)–(7) in an integrated, not piecemeal, review and drafting process to implement policies and procedures responsive to these rules. Therefore, the revised PRA burden estimates no longer account for each requirement as a separate burden.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS, the Commission has preserved the burden estimates from the Proposing Release. The Commission estimates that Rules 17Ad-22(b)(5)–(7) would impose a one-time burden on each respondent CCP of 210 hours, corresponding to an aggregate one-time burden on all respondent CCPs of 1,890 hours.<sup>31</sup>

CCPs would be required to collect information relating to standards of Rules 17Ad-22(b)(5)–(7) on an ongoing basis. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS, the Commission estimates that the ongoing requirements of this rule after the first year would impose an annual burden of 60 hours on each respondent CCP, corresponding to an aggregate annual burden for all respondent CCPs of 540 hours.<sup>32</sup>

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<sup>30</sup> This figure was calculated as follows: Compliance Attorney at 60 hours x 9 respondent CCPs = 540 hours for all respondent CCPs.

For each respondent CCP, the estimated annualized burden for Rule 17Ad-22(b)(4) is 143 hours (figure calculated as follows: 210 hours + 100 hours (Year 1 burden) + 60 hours (Year 2 burden) + 60 hours (Year 3 burden) = 430 hours (estimated total burden over 3 years) ÷ 3 years = 143 hours).

<sup>31</sup> This figure was calculated as follows: ((Assistant General Counsel at 87 hours) + (Compliance Attorney at 77 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 210 hours x 9 respondent CCPs = 1,890 hours.

<sup>32</sup> This figure was calculated as follows: Compliance Attorney at 60 hours x 9 respondent CCPs = 540 hours for all respondent CCPs.

For each respondent CCP, the estimated annualized burden for Rules 17Ad-22(b)(5)–(7) is 110 hours (figure calculated as follows: 210 hours (Year 1 burden) + 60 hours (Year 2 burden) + 60 hours (Year 3 burden) = 330 hours (estimated total burden over 3 years) ÷ 3 years = 110 hours).

### Standards in Rule 17Ad-22(c) that Impose a PRA Burden

The standards in Rule 17Ad-22(c) impose a recordkeeping PRA burden. The requirements of Rule 17Ad-22(c) will apply to all registered clearing agencies. The information collection requirement for Rule 17Ad-22(c) was not discussed separately from Rules 17Ad-22(c)(1)—(2) in the Proposing Release and does not represent a new information collection requirement in the Adopting Release. The burden for Rule 17Ad-22(c) has been separately accounted for in the Adopting Release to reflect the different information collection requirements for varying numbers of respondents.

Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS, the Commission has preserved the burden estimates from the Proposing Release. In contrast to the Proposing Release's burden estimates for proposed Rule 17Ad-22(c)(2), which accounted for 17 clearing agencies, the burden estimate in the adopting release for Rule 17Ad-22(c) reflects a smaller number of clearing agencies. The Commission estimates that Rule 17Ad-22(c) would impose a one-time burden on each respondent clearing agency of 191 hours, corresponding to an aggregate one-time burden on all respondent clearing agencies of 1,910 hours.<sup>33</sup>

The Commission believes the one-time burden imposed would involve adjustments needed to synthesize and format existing information in a manner sufficient to explain the methodology the clearing agency uses to meet the requirement of Rule 17Ad-22(c). The Commission believes these adjustments would impose a one-time burden of 100 hours on each clearing agency, corresponding to an aggregate one-time burden imposed on all clearing agencies of 1,000 hours.<sup>34</sup>

Clearing agencies would be required to collect information relating to standards of Rule 17Ad-22(c) on an ongoing basis. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS, the Commission estimates that the ongoing requirements of this rule would impose an aggregate annual burden of 60 hours on each respondent clearing agency, corresponding to an aggregate annual burden for all respondent clearing agencies of 600 hours.<sup>35</sup>

<sup>33</sup> This figure was calculated as follows: ((Assistant General Counsel at 60 hours) + (Compliance Attorney at 85 hours) + (Computer Operations Manager at 23 hours) + (Senior Business Analyst at 23 hours)) = 191 hours x 10 respondent clearing agencies = 1,910 hours.

<sup>34</sup> This figure was calculated as follows: ((Chief Compliance Officer at 40 hours) + (Computer Operations Department Manager at 40 hours) + (Senior Programmer at 20 hours)) = 100 hours x 10 respondent clearing agencies = 1,000 hours.

<sup>35</sup> This figure was calculated as follows: Compliance Attorney at 60 hours x 10 respondent clearing agencies = 600 hours for all respondent clearing agencies.

For each respondent clearing agency, the estimated annualized burden for Rule 17Ad-22(c) is 137 hours (figure calculated as follows: 191 hours + 100 hours (Year 1 burden) + 60 hours (Year 2 burden) + 60 hours (Year 3 burden) = 411 hours (estimated total burden over 3 years) ÷ 3 years = 137 hours).

### Standards in Rule 17Ad-22(c)(1) that Impose a PRA Burden

The standards in Rule 17Ad-22(c)(1) impose a recordkeeping PRA burden. In contrast to the Proposing Release's burden estimates for proposed Rule 17Ad-22(c)(2), which accounted for 17 clearing agencies, the burden estimate in the adopting release for Rule 17Ad-22(c)(1) reflects a smaller number of clearing agencies. The requirements of Rule 17Ad-22(c)(1) will apply to nine CCPs.

On an ongoing basis, the Commission estimates that for a CCP to generate the required reports concerning its financial resources would impose a burden of three hours per respondent CCP per quarter. This amounts to an annual burden of 12 hours for each CCP and corresponds to an aggregate annual burden of 108 hours for all respondent CCP.<sup>36</sup>

### Standards in Rule 17Ad-22(c)(2) that Impose a PRA Burden

The standards in Rule 17Ad-22(c)(2) impose a third-party disclosure PRA burden. In contrast to the Proposing Release's burden estimates for proposed Rule 17Ad-22(c)(2), which accounted for 17 clearing agencies, the burden estimate in the adopting release for Rule 17Ad-22(c)(2) reflects a smaller number of clearing agencies. The requirements of Rule 17Ad-22(c)(2) will apply to all registered clearing agencies, a total of ten respondents.

With regard to Rule 17Ad-22(c)(2), the requirements will apply to all registered clearing agencies. The Commission expects that the exact burden of collecting information relating to the procedures for facilitating an annual audited financial statement of the clearing agency and posting that annual audited financial statement to the clearing agency's website would vary depending on how frequently each clearing agency may need to update its procedures. Also, the Commission estimates based on its experience with entities of similar size to the respondents to this collection, that the initial burden of generating annual audited financial statements would generally require on average 500 hours per respondent clearing agency.<sup>37</sup> However, as most registered clearing agencies are already implementing this requirement as part of their usual and customary practices, the rule, as an initial burden, would largely affect a total of four entities -- three potential new entrants and one clearing agency that currently does not have two years of annual audited financial statements prepared in accordance with U.S. GAAP or IFRS posted on its website and therefore, would be required to incur the costs of paying for an independent audit

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<sup>36</sup> This figure was calculated as follows: ((Compliance Attorney at 1 hour) + (Computer Operations Department Manager at 2 hours)) = 3 hours per quarter x 4 quarters per year = 12 hours per year x 9 respondent clearing CCPs = 108 hours.

For each respondent CCP, the estimated annualized burden for Rule 17Ad-22(c)(1) is 8 hours (figure calculated as follows: 0 hours (Year 1 burden) + 12 hours (Year 2 burden) + 12 hours (Year 3 burden) = 24 hours (estimated total burden over 3 years) ÷ 3 years = 8 hours).

<sup>37</sup> An example of the Commission's experience with entities of a similar size to the respondents is that the Commission required entities to post their annual financial statements on their respective websites as conditions to the Commission's authorizing them to provide CCP services for credit default swaps.

for two years of financial statements.<sup>38</sup> The Commission estimates that Rule 17Ad-22(c)(2) would impose a one-time burden on each of these four clearing agencies of 500 hours to prepare and review internal financial statements, corresponding to an aggregate one-time burden on the four respondent clearing agencies of 2,000 hours.<sup>39</sup> This requirement would necessitate work hours of compliance personnel and finance personnel at the clearing agency to compile relevant data, organize and analyze that data, and then post it to the clearing agency's website consistent with the rule.

Clearing agencies also would be required to collect information relating to any procedures used to support compliance with Rule 17Ad-22(c)(2) on an ongoing basis. Based on the analogous policies and procedures requirements and the corresponding burden estimates in Regulation NMS, the Commission estimates that the ongoing requirements of this rule would impose an annual burden in subsequent years of 250 hours on each respondent clearing agency for collecting information relating to administering policies and procedures for facilitating an annual audited financial statement of the clearing agency and posting that annual audited financial statement to the clearing agency's website for an aggregate burden of 2,500 hours.<sup>40</sup>

#### Total Burden for Rule 17Ad-22

The total initial burden for Rule 17Ad-22 is 11,340 hours.<sup>41</sup> The total ongoing annual burden for Rule 17Ad-22 is 4,888 hours.<sup>42</sup> When monetized<sup>43</sup> those estimated burdens and costs total \$3.7 million<sup>44</sup> in initial costs and \$10.1 million<sup>45</sup> in annual ongoing costs.

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<sup>38</sup> The Boston Stock Exchange Clearing Corporation ("BSECC") and Stock Clearing Corporation of Philadelphia ("SCCP") currently do not post audited financial statements on their websites and are considered new entrants.

<sup>39</sup> This figure was calculated as follows: Senior Accountant at 500 hours x 4 respondent clearing agencies = 2,000 hours.

<sup>40</sup> This figure was calculated as follows: Senior Accountant at 250 hours x 10 respondent clearing agencies = 2,500 hours.

Annualized, the estimated burden for Rule 17Ad-22(c)(2) is 333 hours (figure calculated as follows: 500 hours (Year 1 burden) + 250 hours (Year 2 burden) + 250 hours (Year 3 burden) = 1,000 hours (estimated total burden over 3 years) ÷ 3 years = 333 hours). This figure represents a weighted average for 10 respondent clearing agencies. The burden will be higher for clearing agencies that have not yet implemented Rule 17Ad-22(c)(2). The burden will be less for clearing agencies that have already implemented the requirement as part of their usual and customary practices.

<sup>41</sup> This figure was calculated as follows: 1,750 hours for initial burdens associated with 17Ad-22(b)(1)–(3) and (d)(1)–(15) + 2,790 hours for initial burdens associated with 17Ad-22(b)(4) + 1,890 hours for initial burdens associated with 17Ad-22(b)(5)–(7) + 4,910 hours for initial burdens associated with 17Ad-22(c) = 11,340 hours.

<sup>42</sup> This figure was calculated as follows: 600 hours for annual burdens associated with 17Ad-22(b)(1)–(3) and (d)(1)–(15) + 540 hours for annual burdens associated with 17Ad-22(b)(4) + 540 hours for annual burdens associated with 17Ad-22(b)(5)–(7) + 3,208 hours for annual burdens associated with 17Ad-22(c) = 4,888 hours.



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43 To monetize the internal costs the Commission staff used data from the SIFMA publications, Management and Professional Earnings in the Security Industry- 2010, and Office Salaries in the Securities Industry – 2010, modified by the Commission staff to account for an 1800 hour work-year and multiplied by 5.35 (professionals) or 2.93 (office) to account for bonuses, firm size, employee benefits and overhead.

44 The total initial cost was calculated as follows: [for Rules 17Ad-22(b)(1)–(3) and (d)(1)–(15) (Assistant General Counsel for 60 hours at \$430 per hour) + (Compliance Attorney for 85 hours at \$320 per hour) + (Computer Operations Department Manager for 15 hours at \$367 per hour) + (Senior Business Analyst for 15 hours at \$232 per hour) = \$61,985 x 10 respondents = \$619,850]; + [for Rule 17Ad-22(b)(4) ((Assistant General Counsel for 87 hours at \$430 per hour) + (Compliance Attorney for 77 hours at \$320 per hour) + (Computer Operations Department Manager for 23 hours at \$367 per hour) + (Senior Business Analyst for 23 hours at \$232 per hour) = \$75,827 x 9 respondents = \$682,443) + ((Chief Compliance Officer for 40 hours at \$423 per hour) + (Computer Department Operations Manager for 40 hours at \$367 per hour) + (Senior Programmer for 20 hours at \$304 per hour) = \$37,680 x 9 respondents = \$339,120) = \$1,021,563]; + [for Rules 17Ad-22(b)(5)–(7) (Assistant General Counsel for 87 hours at \$430 per hour) + (Compliance Attorney for 77 hours at \$320 per hour) + (Computer Operations Department Manager for 23 hours at \$367 per hour) + (Senior Business Analyst for 23 hours at \$232 per hour)) = \$75,827 x 9 respondents = \$682,443]; + [for Rule 17Ad-22(c) ((Assistant General Counsel for 60 hours at \$430 per hour) + (Compliance Attorney for 85 hours at \$320 per hour) + (Computer Operations Department Manager for 23 hours at \$367 per hour) + (Senior Business Analyst for 23 hours at \$232 per hour) = \$66,777 x 10 respondents = \$667,770) + ((Chief Compliance Officer for 40 hours at \$423 per hour) + (Computer Department Operations Manager for 40 hours at \$367 per hour) + (Senior Programmer for 20 hours at \$304 per hour) = \$37,680 x 10 respondents = \$376,800) = \$1,044,570] + [for Rule 17Ad-22(c)(2) (Senior Accountant for 500 hours at \$198 per hour) x 4 respondents = \$396,000] = \$3,764,426.

45 The total ongoing cost was calculated as follows: [for Rules 17Ad-22(b)(1)–(3) and (d)(1)–(15) (Compliance Attorney for 60 hours at \$320 per hour = \$19,200 x 10 respondents = \$192,000)]; + [for Rule 17Ad-22(b)(4) ((Compliance Attorney for 60 hours at \$320 per hour = \$19,200 x 9 respondents = \$172,800) + (2 Independent Consultants for 30 hours per week at \$600 per hour = \$36,000 per week x 12 weeks = \$432,000 x 9 respondents = \$3,888,000) = \$4,060,800]; + [for Rules 17Ad-22(b)(5)–(7) (Compliance Attorney for 60 hours at \$320 per hour = \$19,200 x 9 respondents = \$172,800)]; + [for Rule 17Ad-22(c) (Compliance Attorney for 60 hours at \$320 per hour = \$19,200 x 10 respondents = \$192,000)]; [for Rule 17Ad-22(c)(1) (Compliance Attorney for 1 hour at \$320 per hour) + (Computer Operations Department Manager for 2 hours at \$367) = \$1,054 per quarter x 4 quarters per year = \$4,216 per year x 9 respondents = \$37,944]; [for Rule 17Ad-22(c)(2) (Senior Accountant for 250 hours at \$198 per hour) x 10 respondents = \$495,000) + (Independent Audit Fee = \$500,000 per year x 10 respondents = \$5,000,000)] = \$10,150,544.

Table of Burdens (calculated per respondent)

Rules	Estimated Year 1 Burden	Estimated Year 2 Burden	Estimated Year 3 Burden	Estimated Total Burden over 3 Years	Estimated Annualized Burden/Respondent	Number of Respondents	Total Annualized Burden
Rules 17Ad-22(b)(1)-(3) and (d)(1)-(15)	175 Hours	60 Hours	60 Hours	295 Hours	98 Hours	10	980
Rule 17Ad-22(b)(4)	310 Hours*	60 Hours	60 Hours	430 Hours	143 Hours	9	1287
Rules 17Ad-22(b)(5)-(7)	210 Hours	60 Hours	60 Hours	330 Hours	110 Hours	9	990
Rule 17Ad-22(c)	291 Hours**	60 Hours	60 Hours	411 Hours	137 Hours	10	1370
Rule 17Ad-22(c)(1)		12 Hours	12 Hours	24 Hours	8 Hours	9	72
Rule 17Ad-22(c)(2)	500 Hours	250 Hours	250 Hours	1000 Hours	333 Hours	10	3330
<b>Total</b>	1486 Hours	502 Hours	502 Hours	2490 Hours	829 Hours		8029

### 13. Costs to Respondents

#### Standards in Rule 17Ad-22(b)(4) that Impose Costs

As discussed above, based on its oversight of clearing agencies, the Commission estimates that Rule 17Ad-22(b)(4) would impose an annual cost on all respondent CCPs for work on model validation. Based on its oversight of clearing agencies, the Commission estimates that Rule 17Ad-22(b)(4) would impose an annual cost on all respondent CCPs for work on model validation. The Commission believes clearing agencies would hire a consulting firm that dedicates two consultants to the project. Consistent with the Proposing Release,<sup>46</sup> the Commission estimates that should respondent CCPs decide to hire external consultants to develop and implement Rule 17Ad-22(b)(4) through written policies and procedures, the ongoing cost associated with hiring such consultants would be approximately \$3.9 million per year.<sup>47</sup>

#### Standards in Rule 17Ad-22(c)(2) that Impose Costs

As noted above, Rule 17Ad-22(c)(2) would require each clearing agency to post on its website an annual audited financial statement. The requirement also would require the services of a registered public accounting firm. The Commission estimates those services would on

<sup>46</sup> See Proposing Release, *supra* note 2, at 14529.

<sup>47</sup> This figure was calculated as follows: 2 Consultants for 30 hours per week at \$600 per hour = \$36,000 per week x 12 weeks = \$432,000 per clearing agency x 9 respondent CCPs = \$3,888,000. The \$600 per hour figure for a consultant was calculated using www.payscale.com, modified by Commission staff to account for an 1800 hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead.

average cost approximately \$500,000 annually.<sup>48</sup> Therefore, to meet the ongoing requirements of Rule 17Ad-22(c)(2) the Commission estimates a total annual cost of approximately \$5,000,000 in the aggregate for all respondent clearing agencies.<sup>49</sup>

Total Costs for Rule 17Ad-22

The ongoing external cost for Rule 17Ad-22 is \$8.9 million.<sup>50</sup>

Table of Costs (calculated per respondent)

<b>Rules</b>	<b>Estimated Annualized Cost</b>
<b>Rule 17Ad-22(b)(4)</b>	\$432,000
<b>Rule 17Ad-22(c)(2)</b>	\$500,000
<b>Total</b>	<b>\$932,000</b>

**14. Costs to Federal Government**

Not applicable.

**15. Changes in Burden**

The Commission notes that the PRA burden estimates in the Adopting Release are significantly lower than the PRA burden estimates in the Proposing Release.<sup>51</sup> Several reasons account for the change. The Proposing Release contained five proposed rules with PRA collection of information requirements in addition to Rule 17Ad-22 – proposed Rules 17Aj-1, 17Ad-23, 17Ad-25, 17Ad-26 and 3Cj-1. These other proposed rules are not being adopted at this time.

<sup>48</sup> A precise estimate of audit costs for clearing agencies cannot be made, and therefore, we examined a number of existing surveys, (see, e.g., surveys by CFO.com studying large and small public companies). While the costs may vary depending on the circumstances, we are using an estimate of \$500,000, which is on the upper range for an average cost.

<sup>49</sup> This figure was calculated as follows: \$500,000 estimated cost of registered public accounting firm x 10 respondent clearing agencies = \$5,000,000.

<sup>50</sup> This figure was calculated as follows: \$3,888,000 (for Rule 17Ad-22(b)(4)) + \$5,000,000 (for Rule 17Ad-22(c)(2)).

<sup>51</sup> See Proposing Release at 14521 (“The Commission preliminarily believes that for all respondent clearing agencies the aggregate paperwork burdens contained in proposed Rules 17Ad-22(d)(1), (2), (3), (4), (5), (6), (7), (8), (9), (10), (11), (12), (13), (14), (15), (b)(1), (2), (3), (4), (5), (6), (7), (c)(1) and (2) would impose a one-time burden of 83,343 hours and an ongoing annual burden of 39,658 hours.”). In the Adopting Release, the Commission estimates the total initial burden for Rule 17Ad-22 to be 11,880 hours, with the total ongoing annual burden for Rule 17Ad-22 to be 4,888 hours.

Additionally, the Proposing Release estimated that the proposed rules would have applied to seventeen entities. A number of these entities -- in particular those providing post-trade processing services for security-based swap transactions -- would have been completely unfamiliar with the Commission's registration process for clearing agencies. Further, these entities typically do not have written rule books to govern their relationship with their users. As a result, they would have experienced significant initial burdens associated with the proposed rules.

In contrast, the Rule applies only to the seven clearing agencies currently registered with the Commission that provide CCP or CSD services.<sup>52</sup> These registered clearing agencies already have written rules, policies and procedures addressing significant aspects of Rule 17Ad-22. For purposes of the PRA analysis, the Commission also estimates that three entities may potentially register with the Commission as clearing agencies acting as CCPs, bringing the total number of respondents to ten -- nine of which are CCPs and one of which is a CSD.<sup>53</sup> The Commission believes that some of the entities seeking to register with the Commission as clearing agencies may already be providing similar services in other jurisdictions and therefore may already have written rules and procedures similar to those contemplated by Rule 17Ad-22. Accordingly, the Commission believes that the potential PRA burden on this smaller and more established group of respondents will be significantly lower than the estimates provided in the Proposing Release. Further, the Proposing Release treated each subsection of the rule -- and therefore each required policy and procedure -- as a separate PRA burden. However, the Commission believes that registered clearing agencies are more likely to be able to address the changes required by Rule 17Ad-22 in an integrated, not piecemeal, review and drafting process. That is, respondents are likely to group aspects of Rule 17Ad-22 together as they implement policies and procedures responsive to Rule 17Ad-22. Therefore, the revised PRA burden estimates no longer account for each requirement as a separate burden.

Finally, the Commission has revised the PRA burden estimates in recognition that many parts of Rule 17Ad-22 -- specifically Rules 17Ad-22(b)(1)–(3) and Rules 17Ad-22(d)(1)–(15) -- reflect usual and customary practices of registered clearing agencies. Since registered clearing agencies already comply with significant aspects of Rule 17Ad-22 in the normal course of their activities, many aspects of Rule 17Ad-22 impose minimal PRA burdens on registered clearing agencies limited to the review of the rule and their existing policies and procedures. As discussed below, because certain rules would involve adjustments to a registered clearing agency's rule book and its policies and procedures rather than the creation of entirely separate policies and procedures to support entirely new operations and practices, the Commission recognizes that some aspects of Rule 17Ad-22 will impose incremental new PRA burdens on registered clearing agencies. Accordingly, the estimated PRA burdens discussed below reflect these updated assessments of the likely PRA burdens.

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<sup>52</sup> The Commission also notes that the BSECC and SCCP are currently registered with the Commission as clearing agencies but conduct no clearance or settlement operations. See Securities Exchange Act Release Nos. 63629 (Jan. 3, 2011), 76 FR 1473 (Jan. 10, 2011), and 63268 (Nov. 8, 2010), 75 FR 69730 (Nov. 15, 2010), respectively.

<sup>53</sup> The burden estimates include the possibility that either BSECC or SCCP, or both, resume operations in the future.

**16. Information Planned for Statistical Purposes**

Not applicable.

**17. Approval to Omit OMB Expiration Date**

The Commission is not seeking approval to omit the OMB expiration date.

**18. Exceptions to Certification for Paperwork Reduction Act Submissions**

Not applicable.

**B. COLLECTIONS OF INFORMATION EMPLOYING STATISTICAL METHODS**

Not applicable. The collection of information does not employ statistical methods.