

**SUPPORTING STATEMENT**  
**for the Paperwork Reduction Act Information Collection Submission**

**Rule 18a-3 – Non-cleared security-based swap margin requirements for security-based swap dealers and major security-based swap participants for which there is not a prudential regulator.**

**A. JUSTIFICATION**

**1. Necessity of Information Collection**

In accordance with Section 764 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the “Dodd-Frank Act”), the Securities and Exchange Commission (the “Commission”) has proposed new Rule 18a-3 to set forth minimum margin requirements for nonbank security-based swap dealers (“SBSDs”) and nonbank major security-based swap participants (“MSBSPs”).<sup>1</sup> The rule would establish a new collection of information requirement with respect to SBSDs. The Commission staff estimates that there will be a total of 25 respondents subject at least in part to these new requirements.

Under proposed Rule 18a-3, nonbank SBSDs would be required to monitor the risk of each account and establish, maintain, and document procedures and guidelines for monitoring the risk of accounts as part of its risk management control system required under Rule 15c3-4. In addition, the rule would require nonbank SBSDs to review, in accordance with written procedures and at reasonable periodic intervals, its non-cleared security-based swap activities for consistency with such risk monitoring procedures and guidelines. Nonbank SBSDs would also be required to determine whether information and data necessary to apply the risk monitoring procedures and guidelines are accessible on a timely basis and whether information systems are available to adequately capture, monitor, analyze, and report relevant data and information. Finally, the rule would require that the monitoring procedures and guidelines must include, at a minimum, procedures and guidelines for:

- Obtaining and reviewing account documentation and financial information necessary for assessing the amount of current and potential future exposure to a given counterparty permitted by the SBSD;
- Determining, approving, and periodically reviewing credit limits for each counterparty, and across all counterparties;
- Monitoring credit risk exposure to the SBSD from non-cleared security-based swaps, including the type, scope, and frequency of reporting to senior management;

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<sup>1</sup> See Capital, Margin, and Segregation Requirements for Security-Based Swap Dealers and Major Security-Based Swap Participants and Capital Requirements for Broker-Dealers, Exchange Act Release No. 68071 (Oct. 18, 2012), 77 FR 70213 (Nov. 23, 2012).

- Using stress tests to monitor potential future exposure to a single counterparty and across all counterparties over a specified range of possible market movements over a specified time period;
- Managing the impact of credit exposure related to non-cleared security-based swaps on the SBSB's overall risk exposure;
- Determining the need to collect collateral from a particular counterparty, including whether that determination was based upon the creditworthiness of the counterparty and/or the risk of the specific non-cleared security-based swap contracts with the counterparty;
- Monitoring the credit exposure resulting from concentrated positions with a single counterparty and across all counterparties, and during periods of extreme volatility; and
- Maintaining sufficient equity in the account of each counterparty to protect against the largest individual potential future exposure of a non-cleared security-based swap carried in the account of the counterparty as measured by computing the largest maximum possible loss that could result from the exposure.

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

Information collection under Rule 18a-3 is integral to the Commission's financial responsibility program for nonbank SBSBs. The program is designed to ensure that nonbank SBSBs effectively manage counterparty risk by monitoring their financial exposures to non-cleared security-based swap counterparties. These information collections would facilitate the collection of adequate levels of margin assets by nonbank SBSBs so as to protect them against counterparty default on both current and projected future exposures.

## **3. Consideration Given to Information Technology**

The information collections would not require that respondents use any specific information technology system either to prepare or submit information collections under Rule 18a-3.

## **4. Duplication**

We are not aware of that this information collection duplicates any existing information collection.

## **5. Effect on Small Entities**

The information collections required under Rule 18a-3 would not place burdens on small entities. The nonbank SBSBs that would be subject to the rule are not expected to be small entities.

## **6. Consequences of Not Conducting Collection**

If the required information collections were not conducted or were conducted less frequently, the protection afforded to counterparties and the U.S. financial and banking system would be diminished.

## **7. Inconsistencies with Guidelines in 5 CFR 1320.5(d)(2)**

There are no special circumstances. This collection is consistent with the guidelines 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> A copy of the release is attached. Comments on Commission releases are 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. Any comments received on this proposed rulemaking will be posted on the Commission’s public website, and made available through <http://www.sec.gov/comments/s7-08-12/s70812.shtml>. The Commission will consider all comments received prior to publishing the final rule, and will explain in any adopting release how the final rule responds to such comments, in accordance with 5 C.F.R. 1320.11(f).

## **9. Payment or Gift**

No payment or gift would be provided to respondents.

## **10. Confidentiality**

The information collected by the Commission under Rule 18a-4 would be kept confidential to the extent permitted by the Freedom of Information Act (5 U.S.C. § 552 *et seq.*).

## **11. Sensitive Questions**

No information of a sensitive nature would be required.

## **12. Burden of Information Collection**

The staff estimates that Rule 18a-3 will require in total, on an industry-wide basis, (1) a one-time burden of 5,250 recordkeeping hours, and (2) an annual burden of 1,500 recordkeeping hours.

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<sup>2</sup>

Id.

The Commission staff estimates that there would be 25 nonbank SBSBs<sup>3</sup> that would each spend an average of 210 hours establishing and documenting their Rule 18a-3 counterparty risk monitoring procedures, for a one-time industry-wide hours burden of 5,250 recordkeeping hours.<sup>4</sup> The staff further estimates that each nonbank SBSB would spend an average of 60 hours per year reviewing risks associated with its counterparties, for an annual industry-wide hours burden of 1,500 recordkeeping hours.<sup>5</sup>

### **13. Costs to Respondents**

The staff estimates that 9 out of the 25 nonbank SBSBs would not have previous experience developing margining models (particularly those SBSBs that are not already operating as broker-dealers), and would engage an outside management consultant to review their models, at a rate of \$400 per hour for 5 hours. This would result in a one-time industry-wide external recordkeeping cost of \$6,000,<sup>6</sup> annualized over 3 years.

### **14. Cost to Federal Government**

The staff does not anticipate this information collection to impose additional costs to the Federal Government.

### **15. Changes in Burden**

Not applicable. The information collection is related to a new rule.

### **16. Information Collected Planned for Statistical Purposes**

Not applicable. The information collection is not used for statistical purposes.

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

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

### **18. Exceptions to Certification**

Not applicable. This collection complies with the requirements in 5 CFR 1320.9.

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<sup>3</sup> While Rule 18a-3 contains requirements that apply to both nonbank SBSBs and MSBSPs, the particular requirement that constitutes a collection of information relates only to subpart (e) of the rule, which requires only nonbank SBSBs to establish and follow risk monitoring procedures in respect of individual security-based swap customer agreements. Because this individual account requirement does not apply to MSBSPs, they are not included as respondents in the calculation of the associated burden.

<sup>4</sup> 25 nonbank SBSBs x 210 hrs = 5,250 hrs. These amounts are annualized over three years resulting in 70 hours per nonbank SBSB per year and an industry wide annual burden of 1750 recordkeeping hours.

<sup>5</sup> 25 nonbank SBSBs x 60 hrs = 1,500 hrs.

<sup>6</sup> 9 nonbanks SBSBs x \$400/hr x 5 hrs / 3 years = \$6,000. This amount annualized is \$666.66 per nonbank SBSB.

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

Not applicable. This collection does not employ statistical methods.