

**SUPPORTING STATEMENT for the Paperwork Reduction Act Information Collection
Submission for Rule 18a-2 – Capital requirements for major security-based swap
participants for which there is not a prudential regulator.
3235-0699**

This submission is being made pursuant to the Paperwork Reduction Act of 1995, 44 U.S.C. Section 3501 *et seq.*

A. JUSTIFICATION

1. Necessity of Information Collection

On June 21, 2019, in accordance with Section 764 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”),¹ which added section 15F to the Securities Exchange Act of 1934 (the “Exchange Act”),² the Securities and Exchange Commission (the “Commission”) adopted Rule 18a-2 to establish capital requirements for nonbank major security-based swap participants that are also not registered as broker-dealers (“MSBSPs”).³ In particular, a nonbank MSBSP is required at all times to have and maintain positive tangible net worth. The rule establishes collection of information requirements.

Under Rule 18a-2, as adopted, MSBSPs also need to comply with Rule 15c3-4, which requires OTC derivatives dealers and other firms subject to its provisions to establish, document, and maintain a system of internal risk management controls to assist the firm in managing the risk associated with its business activities, including market, credit, leverage, liquidity, legal, and operational risks.

2. Purpose and Use of the Information Collection

Information collections under Rule 18a-2, as adopted, are integral parts of the Commission’s financial responsibility program for nonbank MSBSPs. The requirement to establish, document, and maintain a system of internal risk management controls will be imposed on MSBSPs because, by definition, they maintain materially large positions in security-based swap markets and will pose substantial risk to the stability of those markets should they default on their obligations. The collections of information in Rule 18a-2, as adopted, will facilitate the monitoring of the financial condition of nonbank MSBSPs by the Commission and its staff.

¹ See *Dodd-Frank Wall Street Reform and Consumer Protection Act*, Public Law 111-203, 124 Stat. 1376 (2010).

² See 15 U.S.C. 78o-10(e)(2)(B).

³ 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. 86175.

3. Consideration Given to Information Technology

The information collections under Rule 18a-2, as adopted, do not require that respondents use any specific information technology system either to prepare or submit information collections under the rule.

4. Duplication

This information collection does not duplicate any existing information collection.

5. Effect on Small Entities

The information collections that are required under Rule 18a-2, as adopted, do not place burdens on small entities. The information collections under the rule are relevant only to market participants whose security-based swap market activity exceeds a large threshold of notional amounts, such that small market participants are exempted.

6. Consequences of Not Conducting Collection

If the required information collections are not conducted or are conducted less frequently, the protection afforded to counterparties and the U.S. financial and 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 requested comment on the collection of information requirements in the proposing release in October 2012.⁴ In addition, in 2018, the Commission reopened the comment period and requested additional comment on the proposed rules and amendments (including potential modifications to proposed rule language).⁵ While the Commission did not receive specific comments with respect to the proposed collection of information with respect to Rule 18a-2, as proposed to be adopted, the Commission received a number of comment letters in response to the 2012 proposal.⁶

9. Payment or Gift

No payment or gift is provided to respondents.

10. Confidentiality

The information that is collected by the Commission under Rule 18a-2, as adopted, is kept confidential to the extent permitted by the Freedom of Information Act (5 U.S.C. § 552 *et seq.*).

11. Sensitive Questions

No questions of a sensitive nature are asked. The information collection does not collect any Personally Identifiable Information (“PII”).⁷ At the same time, however, Commission staff understands that there may be instances when certain information (including, but not limited to, a person’s name, email, or phone number) could be provided by a respondent in response to one of the collections of information. However, Commission staff does not envision any circumstance in which a social security number would be provided pursuant to any of the collections of information. As such, we believe that the treatment of any PII with the collection of information associated with this rule is not likely to implicate the Federal Information Security Management Act of 2002 or the Privacy Act of 1974.

⁴ 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, 70299 (Nov. 23, 2012).

⁵ 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. 84409 (Oct. 11, 2018), 83 FR 53007 (Oct. 19, 2018) (“Capital, Margin, and Segregation Comment Reopening”).

⁶ Comments available at <https://www.sec.gov/comments/s7-08-12/s70812.shtml>.

⁷ The term “Personally Identifiable Information” refers to information which can be used to distinguish or trace an individual’s identity, such as their name, social security number, biometric records, etc. alone, or when combined with other personal or identifying information which is linked or linkable to a specific individual, such as date and place of birth, mother’s maiden name, etc.

12. Burden of Information Collection

The staff estimates that Rule 18a-2, as adopted, will require in total, on an industry-wide basis, (1) a one-time burden of 10,000 recordkeeping hours, and (2) an annual ongoing burden of 1,250 recordkeeping hours.

The staff estimates that 5 or fewer nonbank entities will register with the Commission as MSBSPs. These MSBSPs will be required to establish, document, and regularly review and update risk management control systems with respect to market, credit, leverage, liquidity, legal and operational risks. Based on similar estimates for OTC derivatives dealers, the Commission staff believes that an MSBSP will spend approximately 2,000 hours to implement its risk management control system, resulting in a one-time industry-wide hour burden of 10,000 recordkeeping hours.⁸

Based on similar estimates for OTC derivatives dealers, the staff further estimates that these firms will spend approximately 250 hours per year reviewing and updating their risk management control systems, resulting in an annual industry-wide hour burden of 1,250 recordkeeping hours.⁹

Taken together, the annualized recordkeeping burden for the total industry is 4,583.35 hours.¹⁰

Summary of Hourly Burdens										
Name of Information Collection	Type of Burden	Number of Entities Impacted	Annual Responses per Entity	Initial Burden per Entity per Response	Initial Burden Annualized per Entity per Response	Ongoing Burden per Entity per Response	Annual Burden Per Entity per Response	Total Annual Burden Per Entity	Total Industry Burden	Small Business Entities Affected
Rule 18a-2 (Hour Burden)	Recordkeeping	5	1	2,000	666.67	250	916.67	916.67	4,583.35	0
TOTAL HOURLY BURDEN FOR ALL RESPONDENTS									4,583.35	

13. Costs to Respondents

Because nonbank MSBSPs may not initially have the systems or expertise internally to meet the risk management requirements of Rule 18a-2, as adopted, these firms will likely hire an outside risk management consultant to assist them in implementing their risk management systems. The staff therefore estimates that these firms will hire an outside management consultant for approximately 200 hours, for a one-time external recordkeeping cost of \$80,000

⁸ 5 MSBSPs x 2,000 hours = 10,000 hours. This one-time burden annualized is 3,333.33 hours industry-wide (10,000 hours/3 = 3,333.33) and 666.67 hours per firm (3,333.33/5 MSBSPs = 666.666, rounded to 666.67).

⁹ 5 MSBSPs x 250 hours/year = 1,250 hours/year.

¹⁰ 5 MSBSPs x (2,000 hours/3 years) + 1,250 hours = 4,583.33 hours.

per respondent, or \$26,666.67 per respondent annualized over 3 years, ¹¹ **and a total industry cost of \$400,000, or \$133,333.33¹² annualized over 3 years.**

Nonbank MSBSPs may incur start-up costs to comply with Rule 18a-2, including information technology costs. The information technology systems of a nonbank MSBSP may be in varying stages of readiness to enable these firms to meet the requirements of the rules so the cost of modifying their information technology systems could vary significantly. Based on the estimates for similar collections of information,¹³ the Commission staff expects that a nonbank MSBSP will incur an average of approximately \$16,000 for initial hardware and software external expenses, which, over three years, equals an annualized cost of \$5,333.33 per nonbank MSBSP.¹⁴ This will result in a one-time industry-wide external cost of \$80,000, or \$26,666.67¹⁵ annualized over 3 years. Based on the estimates for these similar collections of information, the average ongoing external cost to meet the requirements of Rule 18a-2 will be approximately \$20,500 per nonbank MSBSP. This will also result in an ongoing annual industry-wide external recordkeeping cost of \$102,500.¹⁶ **Taken together, the annualized cost burden for the total industry is \$129,166.66.**¹⁷

Summary of Dollar Costs										
Name of Information Collection	Type of Burden	Number of Entities Impacted	Annual Responses per Entity	Initial Cost per Entity per Response	Initial Cost Annualized per Entity per Response	Ongoing Cost per Entity per Response	Annual Cost Per Entity per Response	Total Annual Cost Per Entity	Total Industry Cost	Small Business Entities Affected
Rule 18a-2 – Outside management consultant costs	Recordkeeping	5	1	\$80,000	\$26,666.67	0	0	\$26,666.67	\$133,333.35	0
Rule 18a-2 – Information technology costs	Recordkeeping	5	1	\$16,000.00	\$5,333.33	\$20,500.00	\$25,833.33	\$25,833.33	\$129,166.65	0
TOTAL COST FOR ALL RESPONDENTS									\$262,500.00	

14. Cost to Federal Government

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

¹¹ 200 hours * \$400/hour = \$80,000. Annualized, this burden is \$26,666.67 per respondent (\$80,000/3 = \$26,666.667, rounded to \$26, 666.67).

¹² 5 MSBSPs x 200 hours x \$400/hour = \$400,000. Annualized, this industry-wide burden is \$133,333.33 (\$400,000 / 3 years = \$133,333.333, rounded to \$133,333.33).

¹³ See *Risk Management Controls for Broker or Dealers with Market Access*, Exchange Act Release No. 6321 (Nov. 3, 2010), 75 FR 69792, 69814 (Nov. 15, 2010).

¹⁴ \$16,000 / 3 years = \$5,333.333, rounded to \$5,333.33.

¹⁵ 5 MSBSPs x \$16,000 / 3 years = \$26,666.666, rounded to \$26,666.67.

¹⁶ 5 MSBSP x \$20,500 = \$102,500.

¹⁷ 5 MSBSPs x \$16,000 / 3 years + \$102,500 = \$129,166.66.

15. Changes in Burden

There are no changes in burden. However, the cost estimate, which was previously submitted as a single entry, has been separated into two entries in order to explain the estimates more effectively.

16. Information Collected Planned for Statistical Purposes

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

17. OMB Expiration Date Display Approval

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

18. Exceptions to Certification for Paperwork Reduction Act Submissions

This collection complies with the requirements in 5 CFR 1320.9.

B. COLLECTIONS OF INFORMATION EMPLOYING STATISTICAL METHODS

This collection does not involve statistical methods.