

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
(OMB Control No. 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 (17 CFR 240.18a-2) to establish capital requirements for nonbank major security-based swap participants that are also not registered as broker-dealers (“nonbank MSBSPs”).³ In particular, a nonbank MSBSP is required at all times to have and maintain positive tangible net worth. The rule includes collection of information requirements.

Under Rule 18a-2, nonbank MSBSPs also need to comply with Exchange Act Rule 15c3-4 (17 CFR 240.15c3-4), 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 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 nonbank 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.⁴ The collections of information in Rule 18a-2 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.

⁴ The record preservation requirements for the information collections are in Rule 18a-6, 17 CFR 240.18a-6.

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 required Federal Register notice with a 60-day comment period soliciting comments on this collection of information was published. No public comments were received.

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

The Information Collection does not collect information about individuals, therefore, a PIA, SORN, and PAS are not required.

12. Burden of Information Collection

The staff previously estimated that 5 or fewer nonbank entities would register with the Commission as MSBSPs. The staff continues to estimate that 5 or fewer nonbank entities will register with the Commission as MSBSPs, although currently no such entities have registered. These nonbank 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 each nonbank MSBSP will spend approximately 2,000 hours to implement its risk management control system, resulting in a one-time industry-wide hour burden of approximately 10,000 recordkeeping hours, or approximately 3,333 hours per year when annualized over 3 years.⁵

Based on similar estimates for OTC derivatives dealers, the staff further estimates that each of these firms will spend approximately 250 hours per year reviewing and updating its risk management control systems, resulting in an ongoing annual industry-wide hour burden of approximately 1,250 recordkeeping hours per year.⁶

Taken together, the total industry-wide recordkeeping hour burden is approximately 4,583 hours per year.⁷

Summary of Hour Burdens										
Name of Information Collection	Type of Burden	Number of Entities Impacted	Annual Responses per Entity	Initial One-Time Hour Burden Per Entity	Total Initial One-Time Hour Burden	Total Initial One-Time Hour Burden Annualized Over Three Years	Ongoing Annual Hour Burden Per Entity	Total Ongoing Annual Hour Burden	Total Annual Industry Hour Burden	Small Business Entities Affected
Rule 18a-2 (Hour Burden)	Recordkeeping	5	1	2,000	10,000	3,333	250	1,250	4,583	0
TOTAL ANNUAL HOUR BURDEN FOR ALL RESPONDENTS									4,583	

13. Costs to Respondents

(a) Management Consultant Costs: Because nonbank MSBSPs may not initially have the systems or expertise internally to meet the risk management requirements of Rule 18a-2, these firms will likely hire an outside risk management consultant to assist them in implementing their risk management systems. The staff estimates that each firm will hire an outside management consultant for approximately 200 hours at a cost of approximately \$596 per hour, for a one-time

⁵ 5 MSBSPs x 2,000 hours = 10,000 hours. This one-time burden annualized over a 3-year period is approximately 3,333 hours industry-wide (10,000 hours/3 = 3,333.33 rounded down to 3,333).

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

⁷ 2,000 hours/3 years = 3,333.33 + 1,250 hours = 4,583.33 hours rounded down to 4,583.

external management consulting cost of approximately \$119,200 per respondent, and a total one-time industry management consulting cost of approximately \$596,000, or approximately \$198,667 per year⁸ when annualized over 3 years.

(b) Information Technology Costs: 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 Rule 18a-2, so the cost of modifying their information technology systems could vary significantly among firms. Based on estimates for similar collections of information,⁹ the Commission staff expects that each nonbank MSBSP will spend an average of approximately \$16,000 for one-time initial hardware and software external expenses, for a total one-time industry-wide external information technology cost of approximately \$80,000, or approximately \$26,667 per year¹⁰ when annualized over 3 years. Based on the estimates for these similar collections of information, the average ongoing external cost to meet the information technology requirements of Rule 18a-2 will be approximately \$20,500 per nonbank MSBSP. This will also result in an ongoing annual industry-wide external information technology cost of approximately \$102,500.¹¹ Taken together, the total industry-wide information technology related cost burden is approximately \$129,167 per year.¹²

Therefore, the total industry-wide recordkeeping cost burden is approximately \$327,834 per year (\$198,667 + \$129,167 = \$327,834).

Summary of Dollar Costs										
Name of Information Collection	Type of Burden	Number of Entities Impacted	Annual Responses per Entity	Initial One-Time Cost per Entity	Total Initial One-Time Cost	Ongoing Annual Cost per Entity	Total Ongoing Annual Cost	Total Initial One-Time Cost Annualized Over Three Years	Total Annual Industry Cost	Small Business Entities Affected
Rule 18a-2 – Outside management consultant costs	Recordkeeping	5	1	\$119,200	\$596,000	0	0	\$39,733	\$198,667	0
Rule 18a-2 – Information technology costs	Recordkeeping	5	1	\$16,000.00	\$80,000	\$20,500	\$102,500	\$25,833	\$129,167	0
TOTAL ANNUAL COSTS FOR ALL RESPONDENTS									\$327,834	

14. Costs to Federal Government

This information collection does not impose costs on the Federal Government.

⁸ 5 MSBSPs x 200 hours x \$596/hour = \$596,000. Annualized over three years, this industry-wide burden is approximately \$198,667 per year (\$596,000 / 3 years = \$198,666.66 rounded up to \$198,667).

⁹ 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).

¹⁰ 5 MSBSPs x \$16,000 / 3 years = \$26,666.666, rounded up to \$26,667.

¹¹ 5 MSBSP x \$20,500 = \$102,500.

¹² \$80,000 / 3 years + \$102,500 = \$129,166.667 rounded up to \$129,167.

15. Changes in Burden

There are changes to the cost to respondents because due to an increase in estimated management consultant costs, which have risen from an estimate of \$400 an hour to \$596 an hour. As a result, the industry-wide burden has increased from \$400,000 to \$596,000 and the individual burden has increased from \$80,000 to \$119,200.

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

The Commission is not seeking approval to omit the 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.