



DIVISION OF
TRADING AND MARKETS

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

December 22, 2021

Jana Waehrisch
Managing Director
Chris Beatty
Managing Director
Morgan Stanley Europe SE
Grosse Gallusstrasse 18
Frankfurt, Germany 60312

Re: Capital Requirements for Security-Based Swap Dealers

Dear Ms. Waehrisch and Mr. Beatty:

In your December 22, 2021 letter (“Letter”), on behalf of Morgan Stanley Europe SE (“MSESE”), you state that MSESE is not eligible to apply substituted compliance with respect to the capital requirements of Section 15F of the Securities Exchange Act of 1934 (“**Exchange Act**”) and Rules 18a-1, 18a-1a, 18a-1b, 18a-1c, and 18a-1d (“**Exchange Act Capital Requirements**”) thereunder pursuant to the terms and conditions of the order of the U.S. Securities and Exchange Commission (“**Commission**”) granting substituted compliance in connection with certain requirements applicable to security-based swap dealers (“**SBSDs**”) in the Federal Republic of Germany (“**German Order**”).¹ You further state that MSESE also is not eligible to apply substituted compliance with respect to certain recordkeeping requirements of Rules 18a-5 and 18a-6 (“**Linked Recordkeeping Requirements**”), certain reporting requirements of Rule 18a-7 (“**Linked Reporting Requirements**”), and certain notification requirements of Rule 18a-8 (“**Linked Notification Requirements**”) under Section 15F of the Exchange Act because the German Order conditions applying substituted compliance with these requirements on the SBSB applying substituted compliance with respect to the Exchange Act

¹ See Amended and Restated Order Granting Conditional Substituted Compliance in Connection with Certain Requirements Applicable to Non-U.S. Security-Based Swap Dealers and Major Security-Based Swap Participants Subject to Regulation in the Federal Republic of Germany; Amended Orders Addressing Non-U.S. Security-Based Swap Entities Subject to Regulation in the French Republic or the United Kingdom; and Order Extending the Time to Meet Certain Conditions Relating to Capital and Margin, Exchange Act Release No. 93411 (Oct. 22, 2021), 86 FR 59797 (Oct. 28, 2021).

Capital Requirements. For these reasons, you request written assurance that the staff of the Division of Trading and Markets (“**Division staff**”) will not recommend enforcement action to the Commission under the Exchange Act Capital Requirements, Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements during an interim period in which MSESE will take the steps necessary to apply substituted compliance with respect to these requirements pursuant to the terms and conditions of the German Order. Based on the Letter, I understand the following facts and circumstances are relevant to your request.

Background

MSESE

MSESE is an investment firm headquartered in Frankfurt, Germany, and subject to the laws of Germany and the European Union (“**EU**”) governing the activities of investment firms. Its immediate parent company, Morgan Stanley Europe Holdings SE (“**MSEHSE**”) also is headquartered in Frankfurt, Germany. Further, MSESE is the direct 100% owner of Morgan Stanley Bank AG (“**MSBAG**”), a bank headquartered in Frankfurt, Germany.

Pursuant to the Capital Requirements Regulation (“**CRR**”), Article 7 (Derogation from the application of prudential requirements on an individual basis), MSESE has a waiver from complying with German and EU capital requirements (“**Article 7 waiver**”). Under this waiver, MSESE’s immediate holding company – MSEHSE – is subject to and complies with the German and EU capital requirements. In addition, under CRR, Article 8, MSESE consolidates MSBAG for the purposes of complying with German and EU liquidity requirements. As a consequence of this consolidation, any unsecured receivables MSESE has from MSBAG (e.g., cash deposits) are eliminated.

MSESE registered with the Commission as an SBSB on November 1, 2021. In connection with that registration, MSESE filed a notice with the Commission that it would apply substituted compliance with respect to certain Exchange Act requirements pursuant to the terms and conditions of the German Order. However, as discussed in more detail below, MSESE was not eligible to apply substituted compliance with respect to the Exchange Act Capital Requirements, the Linked Recordkeeping Requirements, the Linked Reporting Requirements, and the Linked Notification Requirements because of the Article 7 waiver.

The German Order

On October 22, 2021, the Commission issued the German Order. Paragraph (c)(1) of the German Order makes substituted compliance available with respect to the Exchange Act Capital Requirements, subject to certain conditions.² The first condition is set forth in paragraph

² See German Order, 86 FR at 59816.

(c)(1)(i) of the German Order.³ This condition specifies that the SBSB be subject to and comply with certain German and EU laws prescribing capital, liquidity, and leverage requirements, among other requirements (“**German/EU Law Condition**”).⁴ Currently, MSESE cannot meet the German/EU Law Condition because the Article 7 waiver means it does not have to comply with German and EU capital and leverage requirements set forth in paragraph (c)(1)(i) of the German Order if MSEHSE (the immediate holding company) complies with them on a consolidated basis with MSESE. Under the terms of the Article 7 waiver, MSEHSE is subject to capital, liquidity, and leverage requirements set forth in paragraph (c)(1)(i) of the German Order.⁵ Notwithstanding the Article 7 waiver, MSESE is subject to certain German and EU requirements set forth in paragraph (c)(1)(i) of the German Order, including liquidity requirements on a consolidated basis with MSBAG.⁶

The second condition for applying substituted compliance with respect to the Exchange Act Capital Requirements is set forth in paragraph (c)(1)(ii) of the German Order.⁷ This condition specifies that the SBSB apply substituted compliance with respect to certain Exchange

³ *Id.*

⁴ *Id.* The German and EU laws, as amended from time to time and as defined in the German Order, set forth in paragraph (c)(1)(i) of the German Order are: CRR, Part One (General Provisions) Article 6(1), Part Two (Own Funds), Part Three (Capital Requirements), Part Four (Large Exposures), Part Five (Exposures to Transferred Credit Risk), Part Six (Liquidity), and Part Seven (Leverage); MiFID Org Reg article 23; BRRD, articles 45(6) and 81(1); CRD, articles 73, 79, 86, 129, 129(1), 130, 130(1), 130(5), 131, 133, 133(1), 133(4), 141, 142(1) and (2); EMIR Margin RTS, articles 2, 3(b), 7, and 19(1)(d) and (e), (3) and (8); KWG, sections 10b-10h, 10i(2)-(9), 25a(1) sentence 3 no. 2 and no. 3 b), 33(1) sentence 1c); SAG, sections 49(2), 49d, 62(1), and 138(1); and SolvV, section 37. *See id.* at 59822 (defining these laws).

⁵ In particular, MSEHSE is subject to the following capital requirements specified in paragraph (c)(1)(i) of the German Order: CRR, Part One (General Provisions) Article 6(1), Part Two (Own Funds), Part Three (Capital Requirements), Part Four (Large Exposures), Part Five (Exposures to Transferred Credit Risk), Part Six (Liquidity), and Part Seven (Leverage); MiFID Org Reg article 23; BRRD, articles 45(6) and 81(1); CRD, articles 73, 79, 86, 129, 129(1), 130, 130(1), 130(5), 131, 133, 133(1), 133(4), 141, 142(1) and (2); KWG, sections 10b-10h, 10i(2)-(9), 25a(1) sentence 3 no. 2 and no. 3 b), 33(1) sentence 1c); SAG, sections 49(2), 49d, 62(1), and 138(1); and SolvV, section 37.

⁶ In particular, MSESE is subject to the following requirements specified in paragraph (c)(1)(i) of the German Order (as they are not subject to the Article 7 waiver): CRR, Part Six (Liquidity); MiFID Org Reg article 23; BRRD, article 81(1); EMIR Margin RTS, articles 2, 3(b), 7, and 19(1)(d) and (e), (3) and (8); KWG, section 33(1) sentence 1c); and SAG, section 62(1) and 138(1). MSESE also is subject to CRD Article 87, which requires risks of excessive leverage to be managed.

⁷ *See* German Order, 86 FR at 59816.

Act recordkeeping and notification requirements that are linked to the Exchange Act Capital Requirements (“**Recordkeeping/Notification Condition**”).⁸

The third condition for applying substituted compliance with respect to the Exchange Act Capital Requirements is set forth in paragraph (c)(1)(iii) of the German Order.⁹ This condition has four prongs. The first prong is set forth in paragraph (c)(1)(iii)(A)(1) of the German Order and specifies that the SBSB maintain “liquid assets” (as defined in the German Order) that have an aggregate market value that exceeds the amount of the SBSB’s “adjusted liabilities” (as defined in the German Order) by at least \$100 million before applying a deduction (specified in the German Order) and by at least \$20 million after applying the deduction (“**Net Liquid Assets Test Condition**”).¹⁰

The second prong is set forth in paragraph (c)(1)(iii)(A)(2) of the German Order and specifies that the SBSB make and preserve for three years a quarterly record relating to the Net Liquid Assets Test Condition (“**Quarterly Record Condition**”).¹¹ The third prong is set forth in paragraph (c)(1)(iii)(A)(3) of the German Order and specifies that the SBSB notify the Commission in writing within 24 hours if the firm fails to meet the Net Liquid Assets Test Condition (“**Notification Condition**”).¹² The fourth prong is set forth in paragraph (c)(1)(iii)(A)(4) of the German Order and specifies that the SBSB include its most recent statement of financial condition filed with its local supervisor (whether audited or unaudited) with its initial written notice to the Commission of its intent to rely on substituted compliance as required by the German Order.¹³

The German Order provided that an SBSB has until January 1, 2022 to meet the four-pronged capital condition of paragraph (c)(1)(iii).¹⁴ In addition, the German Order extended the

⁸ *Id.* The recordkeeping and notification requirements are set forth in paragraph (a)(9) of Exchange Act rule 18a-5, paragraph (b)(1)(x) of Exchange Act rule 18a-6, and paragraphs (a)(1)(i), (a)(1)(ii), (b)(1), (b)(2), and (b)(4) of Exchange Act rule 18a-8. As discussed below, applying substituted compliance with respect to these linked recordkeeping and notification requirements is conditioned on the SBSB applying substituted compliance with respect to the Exchange Act Capital Requirements. *See* German Order, 86 FR at 59818-19, 59821. The Recordkeeping/Notification Requirement does the reverse by conditioning substituted compliance with respect to the Exchange Act Capital Requirements on applying substituted compliance with respect to these linked recordkeeping and notification requirements. *See id.* at 59804.

⁹ *See* German Order, 86 FR at 59816.

¹⁰ *Id.*

¹¹ *Id.*

¹² *Id.*

¹³ *Id.*

¹⁴ *See* German Order, 86 FR at 59824.

compliance date for the Exchange Act Capital Requirements for an SBSB in Germany operating pursuant to an Article 7 waiver until January 1, 2022.¹⁵

Paragraphs (f)(1), (f)(2), (f)(3), and (f)(4) of the German Order make substituted compliance available with respect to certain requirements of Rules 18a-5, 18a-6, 18a-7, and 18a-8, respectively.¹⁶ In each case, one of the conditions is that the SBSB be subject to certain specified German and EU recordkeeping, reporting, and notification requirements.¹⁷ MSESE cannot meet certain of these conditions because MSEHSE – rather than MSESE – is subject to the specified German and EU recordkeeping, reporting, and notification requirements because of the Article 7 waiver. In addition, the reporting and notification requirements have conditions that require the SBSB, among other things, to simultaneously send a copy of its annual financial reports and any notifications filed with German or EU authorities to the Commission.¹⁸ With respect to the Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements within these rules, the German Order conditions substituted compliance on the SBSB applying substituted compliance with respect to the Exchange Act Capital Requirements. MSESE cannot meet this condition because of the Article 7 waiver.¹⁹

The Manner and Format Order

Section 15F of the Exchange Act requires SBSBs to “make such reports as are required by the Commission, by rule or regulation, regarding the transactions and positions and financial condition” of the SBSB. In addition, paragraph (a)(1) of Rule 18a-7 (“**Rule 18a-7(a)(1)**”) requires SBSBs for which there is not a prudential regulator to file with the Commission or its

¹⁵ *Id.*

¹⁶ *See* German Order, 86 FR at 59817-21.

¹⁷ *Id.*

¹⁸ *See* German Order, 86 FR at 59821.

¹⁹ The Linked Recordkeeping Requirements are set forth in paragraphs (a)(1), (a)(2), (a)(3), (a)(4), (a)(5), (a)(7), (a)(8), and (a)(9) of Rule 18a-5 and paragraphs (b)(1)(ii), (b)(1)(iii), (b)(1)(v), (b)(1)(vi), (b)(1)(vii), (b)(1)(viii), (b)(1)(ix), (b)(1)(x), (d)(2)(i), and (d)(3)(i) of Rule 18a-6. *See* German Order, 86 FR at 59817-20. The Linked Reporting Requirements are set forth in paragraphs (a)(1), (a)(3), (c), (d), (e), (f), (g), and (h) of Rule 18a-7 and paragraph (j) as applied to paragraphs (a)(1), (a)(3), (c), (d), (e), (f), (g), and (h) of Rule 18a-7. *See* German Order, 86 FR at 59820-21. The Linked Notification Requirements are set forth in paragraphs (a)(1)(i), (a)(1)(ii), (b)(1), (b)(2), (b)(4), and (e) of Rule 18a-8 and paragraph (h) as applied to paragraphs (a)(1)(i), (a)(1)(ii), (b)(1), (b)(2), (b)(4), and (e) of Rule 18a-8. *See* German Order, 86 FR at 59821. In addition, applying substituted compliance with respect to paragraph (b)(1)(viii) of Rule 18a-6 is conditioned on the SBSB applying substituted compliance with respect to the Linked Reporting Requirements and applying substituted compliance with respect to the Linked Reporting Requirements is conditioned on the SBSB applying substituted compliance with respect to paragraph (b)(1)(viii) of Rule 18a-6. *See* German Order, 86 FR 59819-21. MSESE cannot meet these conditions because of the Article 7 waiver.

designee Part II of Form X-17A-5 (“**FOCUS Report Part II**”) within 17 business days after the end of each month.

Paragraph (f)(3)(i) of the German Order makes substituted compliance available with respect to Rule 18a-7(a)(1), subject to four conditions.²⁰ The first condition – set forth in paragraph (f)(3)(i)(A) of the German Order – specifies that the SBSB is subject to and complies with certain German reporting laws.²¹ The second condition – set forth in paragraph (f)(3)(i)(B) of the German Order – specifies that the SBSB files periodic unaudited financial and operational information with the Commission or its designee in the manner and format required by Commission rule or order and presents the financial information in the filing in accordance with generally accepted accounting principles that the SBSB uses to prepare general purpose publicly available or available to be issued financial statements in Germany (“**Local GAAP**”).²² On October 14, 2021, the Commission issued an order specifying how an SBSB must meet the manner and format condition in a substituted compliance order (“**Manner and Format Order**”).²³ The third condition – set forth in in paragraph (f)(3)(i)(C) of the German Order – specifies that the SBSB applies substituted compliance with respect to the Exchange Act Capital requirements (i.e., Rule 18a-7(a)(1) is part of the Linked Reporting Requirements).²⁴ MSESE cannot meet this condition because of the Article 7 waiver. The fourth condition – set forth in in paragraph (f)(3)(i)(D) of the German Order – specifies that the SBSB applies substituted compliance with respect to a recordkeeping requirement that is linked to Rule 18a-7.²⁵

Your Request

The Letter states that MSESE intends to cease operating pursuant to the Article 7 waiver, and instead intends to operate pursuant to the CRR Article 9 for individual consolidation, in order to apply substituted compliance with respect to the Exchange Act Capital Requirements, Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements in accordance with the terms and conditions of the German Order. In order to replace the Article 7 waiver with the alternative approvals under the CRR, specifically an

²⁰ See German Order, 86 FR at 59820.

²¹ *Id.* The German and EU laws, as amended from time to time and as defined in the German Order, set forth in the condition are: CRR articles 99, 394, 430 and Part Six: Title II and Title III; CRR Reporting ITS annexes I, II, III, IV, V, VIII, IX, X, XI, XII and XIII, as applicable.

²² *Id.*

²³ See *Order Specifying the Manner and Format of Filing Unaudited Financial and Operational Information by Security-Based Swap Dealers and Major Security-Based Swap Participants that are not U.S. Persons and are Relying on Substituted Compliance Determinations with Respect to Rule 18a-7*, Exchange Act Release No. 93335 (Oct. 14, 2021), 86 FR 59208 (Oct. 26, 2021).

²⁴ See German Order, 86 FR at 59820.

²⁵ *Id.* Specifically, paragraph (b)(1)(viii) of Rule 18a-6, which is part of the Linked Recordkeeping Requirements.

approval under CRR Article 9 and related approvals for application of other requirements at this level, the Letter states that MSESE will need approvals from, or must otherwise coordinate with, the European Central Bank (“**ECB**”), the Bundesanstalt für Finanzdienstleistungsaufsicht (“**BaFin**”), and the Deutsche Bundesbank (“**Bundesbank**”). The Letter further states that MSESE and similarly situated firms are going through a transition period in which MSESE is first required to be authorized as a CRR credit institution under Article 8 of Directive 2013/36/EU (“**CRD**”) which will on completion lead to a transfer of supervisory responsibility over MSESE from the BaFin to the ECB under the Single Supervisory Mechanism (“**SSM**”). ECB supervision under the SSM is conducted through a Joint Supervisory Team comprising representatives of the ECB, BaFin, and Bundesbank. This means these authorities will be engaged in preparing for that transition at the same time they are considering MSESE’s request to replace the Article 7 waiver with the alternative approvals under the CRR. The Letter states that the ECB has indicated that the process of considering the alternative approvals required to replace the Article 7 waiver would require a full assessment with a decision to be taken post finalization of the authorization process. Consequently, the Letter requests written assurance that the Division staff will not recommend enforcement action to the Commission under the Exchange Act Capital Requirements, Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements if MSESE operates as if it were applying substituted compliance with respect to these requirements until the date that MSESE has taken the necessary steps and obtained the necessary approvals to cease operating pursuant to the Article 7 waiver and, therefore, is able to apply substituted compliance with respect to these requirements pursuant to the terms and conditions of the German Order (“**German Order Compliance Date**”).

In support of this request, the Letter states that MSESE could meet the following terms and conditions of the German Order for applying substituted compliance with respect to the Exchange Act Capital Requirements: (1) the Recordkeeping/Notification Condition of paragraph (c)(1)(ii) of the German Order; (2) the Net Liquid Assets Test Condition of paragraph (c)(1)(iii)(A)(1) of the German Order; (3) the Quarterly Record Condition of paragraph (c)(1)(iii)(A)(2) of the German Order; and (4) the Notification Condition of paragraph (c)(1)(iii)(A)(3) of the German Order. In addition, the Letter states that MSEHSE (the immediate holding company) could meet the following terms and conditions of the German Order: (1) the Net Liquid Assets Test Condition of paragraph (c)(1)(iii)(A)(1) of the German Order; (2) the Quarterly Record Condition of paragraph (c)(1)(iii)(A)(2) of the German Order; and (3) the Notification Condition of paragraph (c)(1)(iii)(A)(3) of the German Order.

The Letter further states that MSESE could meet the terms and conditions for applying substituted compliance with respect to the Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements in paragraphs (f)(1), (f)(2), (f)(3), and (f)(4) of the German Order, other than: (1) the condition that MSESE apply substituted compliance with respect to the Exchange Act Capital Requirements; and (2) certain conditions requiring MSESE to be subject to and comply with related German or EU recordkeeping, reporting, or notification requirements that MSEHSE is subject to because of the Article 7 waiver. The Letter states that MSEHSE could meet the conditions.

In further support of the request, the Letter states that MSESE and MSEHSE could file periodic financial and operational information with the Commission pursuant to the terms and conditions of the Manner and Format Order and present that information in accordance with Local GAAP as if they were applying substituted compliance with respect to Rule 18a-7(a)(1).

Finally, the Letter states that MSESE and MSEHSE could provide the Commission with their most recent statements of financial condition filed with German and EU authorities (whether audited or unaudited) and that MSESE could provide the Commission with a written status update at the end of each month on its progress in taking the necessary steps and obtaining the necessary approvals to become eligible to apply substituted compliance with respect to the Exchange Act Capital Requirements, Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements pursuant to the terms and conditions of the German Order.

Response

Based on the facts and circumstances described in the Letter (and without necessarily agreeing with any conclusions or analysis set forth therein), Division staff will not recommend enforcement action to the Commission under section 15F of the Exchange Act and the Exchange Act Capital Requirements, Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements thereunder because MSESE operates as if it was eligible to apply substituted compliance with respect to these requirements pursuant to the terms and conditions of the German Order; provided that during the period beginning January 1, 2022 and ending on the earlier of (1) the German Order Compliance Date or (2) December 31, 2022 (“**Interim Compliance Period**”):

1. MSESE, on a consolidated or standalone basis, is subject to and complies with CRR, Part Six (Liquidity); CRD Article 87; MiFID Org Reg article 23; BRRD, article 81(1); EMIR Margin RTS, articles 2, 3(b), 7, and 19(1)(d) and (e), (3) and (8); KWG, section 33(1) sentence 1c); and SAG, section 62(1) and 138(1) and submits a written notification to the Commission by email to SBS-OTCDDnotices@sec.gov within 24 hours if it fails to comply with any of these requirements;
2. MSEHSE, on a consolidated basis, is subject to and complies with CRR, Part One (General Provisions) Article 6(1), Part Two (Own Funds), Part Three (Capital Requirements), Part Four (Large Exposures), Part Five (Exposures to Transferred Credit Risk), Part Six (Liquidity), and Part Seven (Leverage); MiFID Org Reg article 23; BRRD, articles 45(6) and 81(1); CRD, articles 73, 79, 86, 129, 129(1), 130, 130(1), 130(5), 131, 133, 133(1), 133(4), 141, 142(1) and (2); KWG, sections 10b-10h, 10i(2)-(9), 25a(1) sentence 3 no. 2 and no. 3 b), 33(1) sentence 1c); SAG, sections 49(2), 49d, 62(1), and 138(1); and SolvV, section 37 and submits a written notification to the Commission by email to SBS-

OTCDDnotices@sec.gov within 24 hours if it fails to comply with any of these requirements;

3. MSESE meets the Recordkeeping/Notification Condition set forth in paragraph (c)(1)(ii) of the German Order;
4. MSESE, on a consolidated basis, meets the Net Liquid Assets Test Condition set forth in paragraph (c)(1)(iii)(A)(1) of the German Order; provided that, after June 30, 2022, MSESE reduces its liquid assets, as defined in paragraph (c)(1)(iii)(B) of the German Order, by the value of any unsecured receivable recognized by MSESE, on an unconsolidated basis, arising from deposits placed with MSBAG or other unsecured receivable exposures to MSBAG;
5. MSEHSE, on a consolidated basis, meets the Net Liquid Assets Test Condition set forth in paragraph (c)(1)(iii)(A)(1) of the German Order;
6. MSESE meets the Quarterly Record Condition set forth in paragraph (c)(1)(iii)(A)(2) of the German Order;
7. MSEHSE meets the Quarterly Record Condition set forth in paragraph (c)(1)(iii)(A)(2) of the German Order;
8. MSESE meets the Notification Condition set forth in paragraph (c)(1)(iii)(A)(3) of the German Order;
9. MSEHSE meets the Notification Condition set forth in paragraph (c)(1)(iii)(A)(3) of the German Order;
10. MSESE submits a copy of its most recent statement of financial condition filed with its local supervisor (whether audited or unaudited) to the Commission by email to SBS-OTCDDnotices@sec.gov during the first week of January 2022;
11. MSEHSE submits a copy of its most recent statement of financial condition filed with its local supervisor (whether audited or unaudited) to the Commission by email to SBS-OTCDDnotices@sec.gov during the first week of January 2022;
12. MSESE files a monthly FOCUS Report Part II with the Commission pursuant to the terms and conditions of the Manner and Format Order and presents the information in the report in accordance with Local GAAP;
13. MSEHSE files a monthly FOCUS Report Part II with the Commission pursuant to the terms and conditions of the Manner and Format Order and presents the information in the report in accordance with Local GAAP;

14. MSESE meets the terms and conditions in the German Order for applying substituted compliance with respect to the Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements, except:
 - (a) For the condition that MSESE applies substituted compliance with respect to the Exchange Act Capital Requirements; and
 - (b) For certain conditions that MSESE is subject to and complies with specified EU and German recordkeeping, reporting, and notification laws that apply to MSEHSE rather than MSESE due to the Article 7 waiver, provided MSEHSE meets the terms and conditions in the German Order for applying substituted compliance with respect to those Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements; and
15. MSESE submits a written status report to the Commission by email to SBS-OTCDDnotices@sec.gov at the end of each month describing its progress in taking the necessary steps and obtaining the necessary approvals to become eligible to meet the terms and conditions for applying substituted compliance with respect to the Exchange Act Capital Requirements, Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements pursuant to the terms and conditions of the German Order.

This Division staff position terminates on the earlier of the German Order Compliance Date or December 31, 2022.

This Division staff position is based strictly on the facts and circumstances stated in the Letter. Any different facts or circumstances from those set forth in the Letter may require a different response. Furthermore, this response expresses Division staff's position on enforcement action only and does not purport to express any legal conclusions on the questions presented. The Division staff expresses no view with respect to any other questions that the proposed activities may raise, including the applicability of any other federal, state, or foreign laws. This position is subject to modification or revocation at any time.

If you have any questions regarding this letter, please contact me at (202) 551-5522.

Sincerely,

Randall W. Roy
Deputy Associate Director
Division of Trading and Markets

December 22, 2021

Jana Waehrisch
Managing Director
Chris Beatty
Managing Director
Morgan Stanley Europe SE
Grosse Gallusstrasse 18
Frankfurt, Germany 60312

Re: Capital Requirements for Security-Based Swap Dealers

Dear Ms. Waehrisch and Mr. Beatty:

In your December 22, 2021 letter (“Letter”), on behalf of Morgan Stanley Europe SE (“MSESE”), you state that MSESE is not eligible to apply substituted compliance with respect to the capital requirements of Section 15F of the Securities Exchange Act of 1934 (“**Exchange Act**”) and Rules 18a-1, 18a-1a, 18a-1b, 18a-1c, and 18a-1d (“**Exchange Act Capital Requirements**”) thereunder pursuant to the terms and conditions of the order of the U.S. Securities and Exchange Commission (“**Commission**”) granting substituted compliance in connection with certain requirements applicable to security-based swap dealers (“**SBSDs**”) in the Federal Republic of Germany (“**German Order**”).¹ You further state that MSESE also is not eligible to apply substituted compliance with respect to certain recordkeeping requirements of Rules 18a-5 and 18a-6 (“**Linked Recordkeeping Requirements**”), certain reporting requirements of Rule 18a-7 (“**Linked Reporting Requirements**”), and certain notification requirements of Rule 18a-8 (“**Linked Notification Requirements**”) under Section 15F of the Exchange Act because the German Order conditions applying substituted compliance with these requirements on the SBSB applying substituted compliance with respect to the Exchange Act Capital Requirements. For these reasons, you request written assurance that the staff of the Division of Trading and Markets (“**Division staff**”) will not recommend enforcement action to the Commission under the Exchange Act Capital Requirements, Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements during an interim period in which MSESE will take the steps necessary to apply substituted compliance with respect to the these requirements pursuant to the terms and conditions of the German Order.

¹ See Amended and Restated Order Granting Conditional Substituted Compliance in Connection with Certain Requirements Applicable to Non-U.S. Security-Based Swap Dealers and Major Security-Based Swap Participants Subject to Regulation in the Federal Republic of Germany; Amended Orders Addressing Non-U.S. Security-Based Swap Entities Subject to Regulation in the French Republic or the United Kingdom; and Order Extending the Time to Meet Certain Conditions Relating to Capital and Margin, Exchange Act Release No. 93411 (Oct. 22, 2021), 86 FR 59797 (Oct. 28, 2021).

Based on the Letter, I understand the following facts and circumstances are relevant to your request.

Background

MSESE

MSESE is an investment firm headquartered in Frankfurt, Germany, and subject to the laws of Germany and the European Union (“EU”) governing the activities of investment firms. Its immediate parent company, Morgan Stanley Europe Holdings SE (“MSEHSE”) also is headquartered in Frankfurt, Germany. Further, MSESE is the direct 100% owner of Morgan Stanley Bank AG (“MSBAG”), a bank headquartered in Frankfurt, Germany.

Pursuant to the Capital Requirements Regulation (“CRR”), Article 7 (Derogation from the application of prudential requirements on an individual basis), MSESE has a waiver from complying with German and EU capital requirements (“Article 7 waiver”). Under this waiver, MSESE’s immediate holding company – MSEHSE – is subject to and complies with the German and EU capital requirements. In addition, under CRR, Article 8, MSESE consolidates MSBAG for the purposes of complying with German and EU liquidity requirements. As a consequence of this consolidation, any unsecured receivables MSESE has from MSBAG (e.g., cash deposits) are eliminated.

MSESE registered with the Commission as an SBSB on November 1, 2021. In connection with that registration, MSESE filed a notice with the Commission that it would apply substituted compliance with respect to certain Exchange Act requirements pursuant to the terms and conditions of the German Order. However, as discussed in more detail below, MSESE was not eligible to apply substituted compliance with respect to the Exchange Act Capital Requirements, the Linked Recordkeeping Requirements, the Linked Reporting Requirements, and the Linked Notification Requirements because of the Article 7 waiver.

The German Order

On October 22, 2021, the Commission issued the German Order. Paragraph (c)(1) of the German Order makes substituted compliance available with respect to the Exchange Act Capital Requirements, subject to certain conditions.² The first condition is set forth in paragraph (c)(1)(i) of the German Order.³ This condition specifies that the SBSB be subject to and comply with certain German and EU laws prescribing capital, liquidity, and leverage requirements, among other requirements (“German/EU Law Condition”).⁴ Currently, MSESE cannot meet

² See German Order, 86 FR at 59816.

³ *Id.*

⁴ *Id.* The German and EU laws, as amended from time to time and as defined in the German Order, set forth in paragraph (c)(1)(i) of the German Order are: CRR, Part One (General Provisions) Article 6(1), Part Two (Own Funds), Part Three (Capital Requirements), Part Four (Large Exposures), Part Five (Exposures to Transferred Credit Risk), Part Six (Liquidity), and Part

the German/EU Law Condition because the Article 7 waiver means it does not have to comply with German and EU capital and leverage requirements set forth in paragraph (c)(1)(i) of the German Order if MSEHSE (the immediate holding company) complies with them on a consolidated basis with MSESE. Under the terms of the Article 7 waiver, MSEHSE is subject to capital, liquidity, and leverage requirements set forth in paragraph (c)(1)(i) of the German Order.⁵ Notwithstanding the Article 7 waiver, MSESE is subject to certain German and EU requirements set forth in paragraph (c)(1)(i) of the German Order, including liquidity requirements on a consolidated basis with MSBAG.⁶

The second condition for applying substituted compliance with respect to the Exchange Act Capital Requirements is set forth in paragraph (c)(1)(ii) of the German Order.⁷ This condition specifies that the SBSB apply substituted compliance with respect to certain Exchange Act recordkeeping and notification requirements that are linked to the Exchange Act Capital Requirements (“**Recordkeeping/Notification Condition**”).⁸

Seven (Leverage); MiFID Org Reg article 23; BRRD, articles 45(6) and 81(1); CRD, articles 73, 79, 86, 129, 129(1), 130, 130(1), 130(5), 131, 133, 133(1), 133(4), 141, 142(1) and (2); EMIR Margin RTS, articles 2, 3(b), 7, and 19(1)(d) and (e), (3) and (8); KWG, sections 10b-10h, 10i(2)-(9), 25a(1) sentence 3 no. 2 and no. 3 b), 33(1) sentence 1c); SAG, sections 49(2), 49d, 62(1), and 138(1); and SolvV, section 37. *See id.* at 59822 (defining these laws).

⁵ In particular, MSEHSE is subject to the following capital requirements specified in paragraph (c)(1)(i) of the German Order: CRR, Part One (General Provisions) Article 6(1), Part Two (Own Funds), Part Three (Capital Requirements), Part Four (Large Exposures), Part Five (Exposures to Transferred Credit Risk), Part Six (Liquidity), and Part Seven (Leverage); MiFID Org Reg article 23; BRRD, articles 45(6) and 81(1); CRD, articles 73, 79, 86, 129, 129(1), 130, 130(1), 130(5), 131, 133, 133(1), 133(4), 141, 142(1) and (2); KWG, sections 10b-10h, 10i(2)-(9), 25a(1) sentence 3 no. 2 and no. 3 b), 33(1) sentence 1c); SAG, sections 49(2), 49d, 62(1), and 138(1); and SolvV, section 37.

⁶ In particular, MSESE is subject to the following requirements specified in paragraph (c)(1)(i) of the German Order (as they are not subject to the Article 7 waiver): CRR, Part Six (Liquidity); MiFID Org Reg article 23; BRRD, article 81(1); EMIR Margin RTS, articles 2, 3(b), 7, and 19(1)(d) and (e), (3) and (8); KWG, section 33(1) sentence 1c); and SAG, section 62(1) and 138(1). MSESE also is subject to CRD Article 87, which requires risks of excessive leverage to be managed.

⁷ *See* German Order, 86 FR at 59816.

⁸ *Id.* The recordkeeping and notification requirements are set forth in paragraph (a)(9) of Exchange Act rule 18a-5, paragraph (b)(1)(x) of Exchange Act rule 18a-6, and paragraphs (a)(1)(i), (a)(1)(ii), (b)(1), (b)(2), and (b)(4) of Exchange Act rule 18a-8. As discussed below, applying substituted compliance with respect to these linked recordkeeping and notification requirements is conditioned on the SBSB applying substituted compliance with respect to the Exchange Act Capital Requirements. *See* German Order, 86 FR at 59818-19, 59821. The Recordkeeping/Notification Requirement does the reverse by conditioning substituted compliance with respect to the Exchange Act Capital Requirements on applying substituted compliance with respect to these linked recordkeeping and notification requirements. *See id.* at 59804.

The third condition for applying substituted compliance with respect to the Exchange Act Capital Requirements is set forth in paragraph (c)(1)(iii) of the German Order.⁹ This condition has four prongs. The first prong is set forth in paragraph (c)(1)(iii)(A)(1) of the German Order and specifies that the SBSB maintain “liquid assets” (as defined in the German Order) that have an aggregate market value that exceeds the amount of the SBSB’s “adjusted liabilities” (as defined in the German Order) by at least \$100 million before applying a deduction (specified in the German Order) and by at least \$20 million after applying the deduction (“**Net Liquid Assets Test Condition**”).¹⁰

The second prong is set forth in paragraph (c)(1)(iii)(A)(2) of the German Order and specifies that the SBSB make and preserve for three years a quarterly record relating to the Net Liquid Assets Test Condition (“**Quarterly Record Condition**”).¹¹ The third prong is set forth in paragraph (c)(1)(iii)(A)(3) of the German Order and specifies that the SBSB notify the Commission in writing within 24 hours if the firm fails to meet the Net Liquid Assets Test Condition (“**Notification Condition**”).¹² The fourth prong is set forth in paragraph (c)(1)(iii)(A)(4) of the German Order and specifies that the SBSB include its most recent statement of financial condition filed with its local supervisor (whether audited or unaudited) with its initial written notice to the Commission of its intent to rely on substituted compliance as required by the German Order.¹³

The German Order provided that an SBSB has until January 1, 2022 to meet the four-pronged capital condition of paragraph (c)(1)(iii).¹⁴ In addition, the German Order extended the compliance date for the Exchange Act Capital Requirements for an SBSB in Germany operating pursuant to an Article 7 waiver until January 1, 2022.¹⁵

Paragraphs (f)(1), (f)(2), (f)(3), and (f)(4) of the German Order make substituted compliance available with respect to certain requirements of Rules 18a-5, 18a-6, 18a-7, and 18a-8, respectively.¹⁶ In each case, one of the conditions is that the SBSB be subject to certain specified German and EU recordkeeping, reporting, and notification requirements.¹⁷ MSESE cannot meet certain of these conditions because MSEHSE – rather than MSESE – is subject to

⁹ See German Order, 86 FR at 59816.

¹⁰ *Id.*

¹¹ *Id.*

¹² *Id.*

¹³ *Id.*

¹⁴ See German Order, 86 FR at 59824.

¹⁵ *Id.*

¹⁶ See German Order, 86 FR at 59817-21.

¹⁷ *Id.*

the specified German and EU recordkeeping, reporting, and notification requirements because of the Article 7 waiver. In addition, the reporting and notification requirements have conditions that require the SBSB, among other things, to simultaneously send a copy of its annual financial reports and any notifications filed with German or EU authorities to the Commission.¹⁸ With respect to the Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements within these rules, the German Order conditions substituted compliance on the SBSB applying substituted compliance with respect to the Exchange Act Capital Requirements. MSESE cannot meet this condition because of the Article 7 waiver.¹⁹

The Manner and Format Order

Section 15F of the Exchange Act requires SBSBs to “make such reports as are required by the Commission, by rule or regulation, regarding the transactions and positions and financial condition” of the SBSB. In addition, paragraph (a)(1) of Rule 18a-7 (“**Rule 18a-7(a)(1)**”) requires SBSBs for which there is not a prudential regulator to file with the Commission or its designee Part II of Form X-17A-5 (“**FOCUS Report Part II**”) within 17 business days after the end of each month.

Paragraph (f)(3)(i) of the German Order makes substituted compliance available with respect to Rule 18a-7(a)(1), subject to four conditions.²⁰ The first condition – set forth in paragraph (f)(3)(i)(A) of the German Order – specifies that the SBSB is subject to and complies with certain German reporting laws.²¹ The second condition – set forth in paragraph (f)(3)(i)(B) of the German Order – specifies that the SBSB files periodic unaudited financial and operational

¹⁸ See German Order, 86 FR at 59821.

¹⁹ The Linked Recordkeeping Requirements are set forth in paragraphs (a)(1), (a)(2), (a)(3), (a)(4), (a)(5), (a)(7), (a)(8), and (a)(9) of Rule 18a-5 and paragraphs (b)(1)(ii), (b)(1)(iii), (b)(1)(v), (b)(1)(vi), (b)(1)(vii), (b)(1)(viii), (b)(1)(ix), (b)(1)(x), (d)(2)(i), and (d)(3)(i) of Rule 18a-6. See German Order, 86 FR at 59817-20. The Linked Reporting Requirements are set forth in paragraphs (a)(1), (a)(3), (c), (d), (e), (f), (g), and (h) of Rule 18a-7 and paragraph (j) as applied to paragraphs (a)(1), (a)(3), (c), (d), (e), (f), (g), and (h) of Rule 18a-7. See German Order, 86 FR at 59820-21. The Linked Notification Requirements are set forth in paragraphs (a)(1)(i), (a)(1)(ii), (b)(1), (b)(2), (b)(4), and (e) of Rule 18a-8 and paragraph (h) as applied to paragraphs (a)(1)(i), (a)(1)(ii), (b)(1), (b)(2), (b)(4), and (e) of Rule 18a-8. See German Order, 86 FR at 59821. In addition, applying substituted compliance with respect to paragraph (b)(1)(viii) of Rule 18a-6 is conditioned on the SBSB applying substituted compliance with respect to the Linked Reporting Requirements and applying substituted compliance with respect to the Linked Reporting Requirements is conditioned on the SBSB applying substituted compliance with respect to paragraph (b)(1)(viii) of Rule 18a-6. See German Order, 86 FR 59819-21. MSESE cannot meet these conditions because of the Article 7 waiver.

²⁰ See German Order, 86 FR at 59820.

²¹ *Id.* The German and EU laws, as amended from time to time and as defined in the German Order, set forth in the condition are: CRR articles 99, 394, 430 and Part Six: Title II and Title III; CRR Reporting ITS annexes I, II, III, IV, V, VIII, IX, X, XI, XII and XIII, as applicable.

information with the Commission or its designee in the manner and format required by Commission rule or order and presents the financial information in the filing in accordance with generally accepted accounting principles that the SBSB uses to prepare general purpose publicly available or available to be issued financial statements in Germany (“**Local GAAP**”).²² On October 14, 2021, the Commission issued an order specifying how an SBSB must meet the manner and format condition in a substituted compliance order (“**Manner and Format Order**”).²³ The third condition – set forth in in paragraph (f)(3)(i)(C) of the German Order – specifies that the SBSB applies substituted compliance with respect to the Exchange Act Capital requirements (i.e., Rule 18a-7(a)(1) is part of the Linked Reporting Requirements).²⁴ MSESE cannot meet this condition because of the Article 7 waiver. The fourth condition – set forth in in paragraph (f)(3)(i)(D) of the German Order – specifies that the SBSB applies substituted compliance with respect to a recordkeeping requirement that is linked to Rule 18a-7.²⁵

Your Request

The Letter states that MSESE intends to cease operating pursuant to the Article 7 waiver, and instead intends to operate pursuant to the CRR Article 9 for individual consolidation, in order to apply substituted compliance with respect to the Exchange Act Capital Requirements, Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements in accordance with the terms and conditions of the German Order. In order to replace the Article 7 waiver with the alternative approvals under the CRR, specifically an approval under CRR Article 9 and related approvals for application of other requirements at this level, the Letter states that MSESE will need approvals from, or must otherwise coordinate with, the European Central Bank (“**ECB**”), the Bundesanstalt für Finanzdienstleistungsaufsicht (“**BaFin**”), and the Deutsche Bundesbank (“**Bundesbank**”). The Letter further states that MSESE and similarly situated firms are going through a transition period in which MSESE is first required to be authorized as a CRR credit institution under Article 8 of Directive 2013/36/EU (“**CRD**”) which will on completion lead to a transfer of supervisory responsibility over MSESE from the BaFin to the ECB under the Single Supervisory Mechanism (“**SSM**”). ECB supervision under the SSM is conducted through a Joint Supervisory Team comprising representatives of the ECB, BaFin, and Bundesbank. This means these authorities will be engaged in preparing for that transition at the same time they are considering MSESE’s request to replace the Article 7 waiver with the alternative approvals under the CRR. The Letter states that the ECB has indicated that the process of considering the alternative approvals required to

²² *Id.*

²³ *See Order Specifying the Manner and Format of Filing Unaudited Financial and Operational Information by Security-Based Swap Dealers and Major Security-Based Swap Participants that are not U.S. Persons and are Relying on Substituted Compliance Determinations with Respect to Rule 18a-7*, Exchange Act Release No. 93335 (Oct. 14, 2021), 86 FR 59208 (Oct. 26, 2021).

²⁴ *See German Order*, 86 FR at 59820.

²⁵ *Id.* Specifically, paragraph (b)(1)(viii) of Rule 18a-6, which is part of the Linked Recordkeeping Requirements.

replace the Article 7 waiver would require a full assessment with a decision to be taken post finalization of the authorization process. Consequently, the Letter requests written assurance that the Division staff will not recommend enforcement action to the Commission under the Exchange Act Capital Requirements, Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements if MSESE operates as if it were applying substituted compliance with respect to these requirements until the date that MSESE has taken the necessary steps and obtained the necessary approvals to cease operating pursuant to the Article 7 waiver and, therefore, is able to apply substituted compliance with respect to these requirements pursuant to the terms and conditions of the German Order (“**German Order Compliance Date**”).

In support of this request, the Letter states that MSESE could meet the following terms and conditions of the German Order for applying substituted compliance with respect to the Exchange Act Capital Requirements: (1) the Recordkeeping/Notification Condition of paragraph (c)(1)(ii) of the German Order; (2) the Net Liquid Assets Test Condition of paragraph (c)(1)(iii)(A)(1) of the German Order; (3) the Quarterly Record Condition of paragraph (c)(1)(iii)(A)(2) of the German Order; and (4) the Notification Condition of paragraph (c)(1)(iii)(A)(3) of the German Order. In addition, the Letter states that MSEHSE (the immediate holding company) could meet the following terms and conditions of the German Order: (1) the Net Liquid Assets Test Condition of paragraph (c)(1)(iii)(A)(1) of the German Order; (2) the Quarterly Record Condition of paragraph (c)(1)(iii)(A)(2) of the German Order; and (3) the Notification Condition of paragraph (c)(1)(iii)(A)(3) of the German Order.

The Letter further states that MSESE could meet the terms and conditions for applying substituted compliance with respect to the Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements in paragraphs (f)(1), (f)(2), (f)(3), and (f)(4) of the German Order, other than: (1) the condition that MSESE apply substituted compliance with respect to the Exchange Act Capital Requirements; and (2) certain conditions requiring MSESE to be subject to and comply with related German or EU recordkeeping, reporting, or notification requirements that MSEHSE is subject to because of the Article 7 waiver. The Letter states that MSEHSE could meet the conditions.

In further support of the request, the Letter states that MSESE and MSEHSE could file periodic financial and operational information with the Commission pursuant to the terms and conditions of the Manner and Format Order and present that information in accordance with Local GAAP as if they were applying substituted compliance with respect to Rule 18a-7(a)(1).

Finally, the Letter states that MSESE and MSEHSE could provide the Commission with their most recent statements of financial condition filed with German and EU authorities (whether audited or unaudited) and that MSESE could provide the Commission with a written status update at the end of each month on its progress in taking the necessary steps and obtaining the necessary approvals to become eligible to apply substituted compliance with respect to the Exchange Act Capital Requirements, Linked Recordkeeping Requirements, Linked Reporting

Requirements, and Linked Notification Requirements pursuant to the terms and conditions of the German Order.

Response

Based on the facts and circumstances described in the Letter (and without necessarily agreeing with any conclusions or analysis set forth therein), Division staff will not recommend enforcement action to the Commission under section 15F of the Exchange Act and the Exchange Act Capital Requirements, Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements thereunder because MSESE operates as if it was eligible to apply substituted compliance with respect to these requirements pursuant to the terms and conditions of the German Order; provided that during the period beginning January 1, 2022 and ending on the earlier of (1) the German Order Compliance Date or (2) December 31, 2022 (“**Interim Compliance Period**”):

1. MSESE, on a consolidated or standalone basis, is subject to and complies with CRR, Part Six (Liquidity); CRD Article 87; MiFID Org Reg article 23; BRRD, article 81(1); EMIR Margin RTS, articles 2, 3(b), 7, and 19(1)(d) and (e), (3) and (8); KWG, section 33(1) sentence 1c); and SAG, section 62(1) and 138(1) and submits a written notification to the Commission by email to SBS-OTCDDnotices@sec.gov within 24 hours if it fails to comply with any of these requirements;
2. MSEHSE, on a consolidated basis, is subject to and complies with CRR, Part One (General Provisions) Article 6(1), Part Two (Own Funds), Part Three (Capital Requirements), Part Four (Large Exposures), Part Five (Exposures to Transferred Credit Risk), Part Six (Liquidity), and Part Seven (Leverage); MiFID Org Reg article 23; BRRD, articles 45(6) and 81(1); CRD, articles 73, 79, 86, 129, 129(1), 130, 130(1), 130(5), 131, 133, 133(1), 133(4), 141, 142(1) and (2); KWG, sections 10b-10h, 10i(2)-(9), 25a(1) sentence 3 no. 2 and no. 3 b), 33(1) sentence 1c); SAG, sections 49(2), 49d, 62(1), and 138(1); and SolvV, section 37 and submits a written notification to the Commission by email to SBS-OTCDDnotices@sec.gov within 24 hours if it fails to comply with any of these requirements;
3. MSESE meets the Recordkeeping/Notification Condition set forth in paragraph (c)(1)(ii) of the German Order;
4. MSESE, on a consolidated basis, meets the Net Liquid Assets Test Condition set forth in paragraph (c)(1)(iii)(A)(I) of the German Order; provided that, after June 30, 2022, MSESE reduces its liquid assets, as defined in paragraph (c)(1)(iii)(B) of the German Order, by the value of any unsecured receivable recognized by MSESE, on an unconsolidated basis, arising from deposits placed with MSBAG or other unsecured receivable exposures to MSBAG;

5. MSEHSE, on a consolidated basis, meets the Net Liquid Assets Test Condition set forth in paragraph (c)(1)(iii)(A)(1) of the German Order;
6. MSESE meets the Quarterly Record Condition set forth in paragraph (c)(1)(iii)(A)(2) of the German Order;
7. MSEHSE meets the Quarterly Record Condition set forth in paragraph (c)(1)(iii)(A)(2) of the German Order;
8. MSESE meets the Notification Condition set forth in paragraph (c)(1)(iii)(A)(3) of the German Order;
9. MSEHSE meets the Notification Condition set forth in paragraph (c)(1)(iii)(A)(3) of the German Order;
10. MSESE submits a copy of its most recent statement of financial condition filed with its local supervisor (whether audited or unaudited) to the Commission by email to SBS-OTCDDnotices@sec.gov during the first week of January 2022;
11. MSEHSE submits a copy of its most recent statement of financial condition filed with its local supervisor (whether audited or unaudited) to the Commission by email to SBS-OTCDDnotices@sec.gov during the first week of January 2022;
12. MSESE files a monthly FOCUS Report Part II with the Commission pursuant to the terms and conditions of the Manner and Format Order and presents the information in the report in accordance with Local GAAP;
13. MSEHSE files a monthly FOCUS Report Part II with the Commission pursuant to the terms and conditions of the Manner and Format Order and presents the information in the report in accordance with Local GAAP;
14. MSESE meets the terms and conditions in the German Order for applying substituted compliance with respect to the Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements, except:
 - (a) For the condition that MSESE applies substituted compliance with respect to the Exchange Act Capital Requirements; and
 - (b) For certain conditions that MSESE is subject to and complies with specified EU and German recordkeeping, reporting, and notification laws that apply to MSEHSE rather than MSESE due to the Article 7 waiver, provided MSEHSE meets the terms and conditions in the German Order for applying substituted compliance with respect to those Linked

Recordkeeping Requirements, Linked Reporting Requirements, and
Linked Notification Requirements; and

15. MSESE submits a written status report to the Commission by email to SBS-OTCDDnotices@sec.gov at the end of each month describing its progress in taking the necessary steps and obtaining the necessary approvals to become eligible to meet the terms and conditions for applying substituted compliance with respect to the Exchange Act Capital Requirements, Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements pursuant to the terms and conditions of the German Order.

This Division staff position terminates on the earlier of the German Order Compliance Date or December 31, 2022.

This Division staff position is based strictly on the facts and circumstances stated in the Letter. Any different facts or circumstances from those set forth in the Letter may require a different response. Furthermore, this response expresses Division staff's position on enforcement action only and does not purport to express any legal conclusions on the questions presented. The Division staff expresses no view with respect to any other questions that the proposed activities may raise, including the applicability of any other federal, state, or foreign laws. This position is subject to modification or revocation at any time.

If you have any questions regarding this letter, please contact me at (202) 551-5522.

Sincerely,

Randall W. Roy
Deputy Associate Director
Division of Trading and Markets

Morgan Stanley Europe SE

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Morgan Stanley

December 22, 2021

Randall W. Roy
Deputy Associate Director
Division of Trading and Markets
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

Re: Extension request for Article 7 SBSDs' compliance with paragraph (c)(1) of the German Order

Dear Mr. Roy:

On behalf of Morgan Stanley Europe SE ("MSESE"), I am requesting written assurance that the staff of the Division of Trading and Markets ("**Division staff**") of the U.S. Securities and Exchange Commission ("**Commission**") will not recommend enforcement action to the Commission under Section 15F of the Securities Exchange Act of 1934 ("**Exchange Act**") and the capital requirements of Rules 18a-1 and 18a-1a through 18a-1d, certain recordkeeping requirements of Rules 18a-5 and 18a-6, certain reporting requirements of Rule 18a-7, and certain notification requirements of Rule 18a-8 while MSESE takes the necessary steps and obtains the necessary approvals to apply substituted compliance with respect to these requirements pursuant to all the terms and conditions of the Commission's order granting substituted compliance in connection with certain requirements applicable to security-based swap dealers ("**SBSDs**") in the Federal Republic of Germany ("**German Order**").¹

¹ See Amended and Restated Order Granting Conditional Substituted Compliance in Connection with Certain Requirements Applicable to Non-U.S. Security-Based Swap Dealers and Major Security-Based Swap Participants Subject to Regulation in the Federal Republic of Germany; Amended Orders Addressing Non-U.S. Security-Based Swap Entities Subject to Regulation in the French Republic or the United Kingdom; and Order Extending the Time to Meet Certain Conditions Relating to Capital and Margin. Exchange Act Release No. 93411 (Oct. 22, 2021), 86 FR 59797 (Oct. 28, 2021).

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Background

MSESE

MSESE is an investment firm headquartered in Frankfurt, Germany, and subject to the laws of Germany and the European Union (“EU”) governing the activities of investment firms. Its immediate parent company, Morgan Stanley Europe Holdings SE (“MSEHSE”) also is headquartered in Frankfurt, Germany. Further, MSESE is the direct 100% owner of Morgan Stanley Bank AG (“MSBAG”), a bank headquartered in Frankfurt, Germany.

Pursuant to the Capital Requirements Regulation (“CRR”), Article 7 (Derogation from the application of prudential requirements on an individual basis), MSESE has a waiver from complying with German and EU capital requirements (“**Article 7 waiver**”). Under this waiver, MSESE’s immediate holding company – MSEHSE – is subject to and complies with the German and EU capital requirements. In addition, under CRR, Article 8, MSESE consolidates MSBAG for the purposes of complying with German and EU liquidity requirements. As a consequence of this consolidation, any unsecured receivables MSESE has from MSBAG (e.g., cash deposits) are eliminated.

MSESE registered with the Commission as an SBSB on November 1, 2021. In connection with that registration, MSESE filed a notice with the Commission that it would apply substituted compliance with respect to certain Exchange Act requirements pursuant to the terms and conditions of the German Order. However, as discussed in more detail below, MSESE was not eligible to apply substituted compliance with respect to Rules 18a-1, 18a-1a, 18a-1b, 18a-1c, and 18a-1d (“**Exchange Act Capital Requirements**”), certain recordkeeping requirements of Rules 18a-5 and 18a-6 (“**Linked Recordkeeping Requirements**”), certain reporting requirements of Rule 18a-7 (“**Linked Reporting Requirements**”), and certain notification requirements of Rule 18a-8 (“**Linked Notification Requirements**”) due to the Article 7 waiver.

The German Order

On October 22, 2021, the Commission issued the German Order. Paragraph (c)(1) of the German Order makes substituted compliance available with respect to the Exchange Act Capital Requirements, subject to certain conditions.² The first condition is set forth in paragraph (c)(1)(i) of the German Order.³ This condition specifies that the SBSB be subject

² See German Order, 86 FR at 59816.

³ *Id.*

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to and comply with certain German and EU laws prescribing capital, liquidity, and leverage requirements, among other requirements (“**German/EU Law Condition**”).⁴ Currently, MSESE cannot meet the German/EU Law Condition because the Article 7 waiver means it does not have to comply with German and EU capital and leverage requirements set forth in paragraph (c)(1)(i) of the German Order if MSEHSE (the immediate holding company) complies with them on a consolidated basis with MSESE. Under the terms of the Article 7 waiver, MSEHSE is subject to capital, liquidity, and leverage requirements set forth in paragraph (c)(1)(i) of the German Order.⁵ Notwithstanding the Article 7 waiver, MSESE is subject to certain German and EU requirements set forth in paragraph (c)(1)(i) of the German Order, including liquidity requirements on a consolidated basis with MSBAG.⁶

The second condition for applying substituted compliance with respect to the Exchange Act Capital Requirements is set forth in paragraph (c)(1)(ii) of the German Order.⁷ This condition specifies that the SBSB apply substituted compliance with respect to certain Exchange Act recordkeeping and notification requirements that are linked to the Exchange Act Capital Requirements (“**Recordkeeping/Notification Condition**”).⁸

⁴ *Id.* The German and EU laws, as amended from time to time and as defined in the German Order, set forth in paragraph (c)(1)(i) of the German Order are: CRR, Part One (General Provisions) Article 6(1), Part Two (Own Funds), Part Three (Capital Requirements), Part Four (Large Exposures), Part Five (Exposures to Transferred Credit Risk), Part Six (Liquidity), and Part Seven (Leverage); MiFID Org Reg article 23; BRRD, articles 45(6) and 81(1); CRD, articles 73, 79, 86, 129, 129(1), 130, 130(1), 130(5), 131, 133, 133(1), 133(4), 141, 142(1) and (2); EMIR Margin RTS, articles 2, 3(b), 7, and 19(1)(d) and (e), (3) and (8); KWG, sections 10b-10h, 10i(2)-(9), 25a(1) sentence 3 no. 2 and no. 3 b), 33(1) sentence 1c); SAG, sections 49(2), 49d, 62(1), and 138(1); and SolvV, section 37. *See id.* at 59822 (defining these laws).

⁵ In particular, MSEHSE is subject to the following capital requirements specified in paragraph (c)(1)(i) of the German Order: CRR, Part One (General Provisions) Article 6(1), Part Two (Own Funds), Part Three (Capital Requirements), Part Four (Large Exposures), Part Five (Exposures to Transferred Credit Risk), Part Six (Liquidity), and Part Seven (Leverage); MiFID Org Reg article 23; BRRD, articles 45(6) and 81(1); CRD, articles 73, 79, 86, 129, 129(1), 130, 130(1), 130(5), 131, 133, 133(1), 133(4), 141, 142(1) and (2); KWG, sections 10b-10h, 10i(2)-(9), 25a(1) sentence 3 no. 2 and no. 3 b), 33(1) sentence 1c); SAG, sections 49(2), 49d, 62(1), and 138(1); and SolvV, section 37.

⁶ In particular, MSESE is subject to the following requirements specified in paragraph (c)(1)(i) of the German Order (as they are not subject to the Article 7 waiver): CRR, Part Six (Liquidity); MiFID Org Reg article 23; BRRD, article 81(1); EMIR Margin RTS, articles 2, 3(b), 7, and 19(1)(d) and (e), (3) and (8); KWG, section 33(1) sentence 1c); and SAG, section 62(1) and 138(1). MSESE also is subject to CRD Article 87, which requires risks of excessive leverage to be managed.

⁷ *See* German Order, 86 FR at 59816.

⁸ *Id.* The recordkeeping and notification requirements are set forth in paragraph (a)(9) of Exchange Act rule 18a-5, paragraph (b)(1)(x) of Exchange Act rule 18a-6, and paragraphs (a)(1)(i), (a)(1)(ii), (b)(1), (b)(2), and (b)(4) of Exchange Act rule 18a-8. As discussed below, applying substituted compliance with respect to these linked recordkeeping and notification requirements is conditioned on the SBSB

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The third condition for applying substituted compliance with respect to the Exchange Act Capital Requirements is set forth in paragraph (c)(1)(iii) of the German Order.⁹ This condition has four prongs. The first prong is set forth in paragraph (c)(1)(iii)(A)(1) of the German Order and specifies that the SBSB maintain “liquid assets” (as defined in the German Order) that have an aggregate market value that exceeds the amount of the SBSB’s “adjusted liabilities” (as defined in the German Order) by at least \$100 million before applying a deduction (specified in the German Order) and by at least \$20 million after applying the deduction (“**Net Liquid Assets Test Condition**”).¹⁰

The second prong is set forth in paragraph (c)(1)(iii)(A)(2) of the German Order and specifies that the SBSB make and preserve for three years a quarterly record relating to the Net Liquid Assets Test Condition (“**Quarterly Record Condition**”).¹¹ The third prong is set forth in paragraph (c)(1)(iii)(A)(3) of the German Order and specifies that the SBSB notify the Commission in writing within 24 hours if the firm fails to meet the Net Liquid Assets Test Condition (“**Notification Condition**”).¹² The fourth prong is set forth in paragraph (c)(1)(iii)(A)(4) of the German Order and specifies that the SBSB include its most recent statement of financial condition filed with its local supervisor (whether audited or unaudited) with its initial written notice to the Commission of its intent to rely on substituted compliance as required by the German Order.¹³

The German Order provided that an SBSB has until January 1, 2022 to meet the four-pronged capital condition of paragraph (c)(1)(iii).¹⁴ In addition, the German Order extended the compliance date for the Exchange Act Capital Requirements for an SBSB in Germany operating pursuant to an Article 7 waiver until January 1, 2022.¹⁵

applying substituted compliance with respect to the Exchange Act Capital Requirements. *See* German Order, 86 FR at 59818-19, 59821. The Recordkeeping/Notification Requirement does the reverse by conditioning substituted compliance with respect to the Exchange Act Capital Requirements on applying substituted compliance with respect to these linked recordkeeping and notification requirements. *See id.* at 59804.

⁹ *See* German Order, 86 FR at 59816.

¹⁰ *Id.*

¹¹ *Id.*

¹² *Id.*

¹³ *Id.*

¹⁴ *See* German Order, 86 FR at 59824.

¹⁵ *Id.*

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Paragraphs (f)(1), (f)(2), (f)(3), and (f)(4) of the German Order make substituted compliance available with respect to certain requirements of Rules 18a-5, 18a-6, 18a-7, and 18a-8, respectively.¹⁶ In each case, one of the conditions is that the SBSB be subject to certain specified German and EU recordkeeping, reporting, and notification requirements.¹⁷ MSESE cannot meet certain of these conditions because MSEHSE – rather than MSESE – is subject to the specified German and EU recordkeeping, reporting, and notification requirements because of the Article 7 waiver. In addition, the reporting and notification requirements have conditions that the SBSB, among other things, simultaneously send a copy of its annual financial reports and any notifications filed with German or EU authorities to the Commission.¹⁸ With respect to the Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements within these rules, the German Order conditions substituted compliance on the SBSB applying substituted compliance with respect to the Exchange Act Capital Requirements. MSESE cannot meet this condition because of the Article 7 waiver.¹⁹

The Manner and Format Order

Section 15F of the Exchange Act requires SBSBs to “make such reports as are required by the Commission, by rule or regulation, regarding the transactions and positions and financial condition” of the SBSB. In addition, paragraph (a)(1) of Rule 18a-7 (“**Rule 18a-7(a)(1)**”) requires SBSBs for which there is not a prudential regulator to file with the Commission or its designee Part II of Form X-17A-5 (“**FOCUS Report Part II**”) within 17 business days after the end of each month.

¹⁶ See German Order, 86 FR at 59817-21.

¹⁷ *Id.*

¹⁸ See German Order, 86 FR at 59821.

¹⁹ The Linked Recordkeeping Requirements are set forth in paragraphs (a)(1), (a)(2), (a)(3), (a)(4), (a)(5), (a)(7), (a)(8), and (a)(9) of Rule 18a-5 and paragraphs (b)(1)(ii), (b)(1)(iii), (b)(1)(v), (b)(1)(vi), (b)(1)(vii), (b)(1)(viii), (b)(1)(ix), (b)(1)(x), (d)(2)(i), and (d)(3)(i) of Rule 18a-6. See German Order, 86 FR at 59817-20. The Linked Reporting Requirements are set forth in paragraphs (a)(1), (a)(3), (c), (d), (e), (f), (g), and (h) of Rule 18a-7 and paragraph (j) as applied to paragraphs (a)(1), (a)(3), (c), (d), (e), (f), (g), and (h) of Rule 18a-7. See German Order, 86 FR at 59820-21. The Linked Notification Requirements are set forth in paragraphs (a)(1)(i), (a)(1)(ii), (b)(1), (b)(2), (b)(4), and (e) of Rule 18a-8 and paragraph (h) as applied to paragraphs (a)(1)(i), (a)(1)(ii), (b)(1), (b)(2), (b)(4), and (e) of Rule 18a-8. See German Order, 86 FR at 59821. In addition, applying substituted compliance with respect to paragraph (b)(1)(viii) of Rule 18a-6 is conditioned on the SBSB applying substituted compliance with respect to the Linked Reporting Requirements and applying substituted compliance with respect to the Linked Reporting Requirements is conditioned on the SBSB applying substituted compliance with respect to paragraph (b)(1)(viii) of Rule 18a-6. See German Order, 86 FR 59819-21. MSESE cannot meet these conditions because of the Article 7 waiver.

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Paragraph (f)(3)(i) of the German Order makes substituted compliance available with respect to Rule 18a-7(a)(1), subject to four conditions.²⁰ The first condition – set forth in paragraph (f)(3)(i)(A) of the German Order – specifies that the SBSB is subject to and complies with certain German reporting laws.²¹ The second condition – set forth in paragraph (f)(3)(i)(B) of the German Order – specifies that the SBSB files periodic unaudited financial and operational information with the Commission or its designee in the manner and format required by Commission rule or order and presents the financial information in the filing in accordance with generally accepted accounting principles that the SBSB uses to prepare general purpose publicly available or available to be issued financial statements in Germany (“**Local GAAP**”).²² On October 14, 2021, the Commission issued an order specifying how an SBSB must meet the manner and format condition in a substituted compliance order (“**Manner and Format Order**”).²³ The third condition – set forth in in paragraph (f)(3)(i)(C) of the German Order – specifies that the SBSB applies substituted compliance with respect to the Exchange Act Capital requirements (i.e., Rule 18a-7(a)(1) is part of the Linked Reporting Requirements).²⁴ MSESE cannot meet this condition because of the Article 7 waiver. The fourth condition – set forth in in paragraph (f)(3)(i)(D) of the German Order – specifies that the SBSB applies substituted compliance with respect to a recordkeeping requirement that is linked to Rule 18a-7.²⁵

Request

MSESE intends to cease operating pursuant to the Article 7 waiver, and instead intends to operate pursuant to the CRR Article 9 for individual consolidation, in order to apply substituted compliance with respect to the Exchange Act Capital Requirements, Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements in accordance with the terms and conditions of the German Order. In order to replace the Article 7 waiver with the alternative approvals under the CRR, specifically an

²⁰ See German Order, 86 FR at 59820.

²¹ *Id.* The German and EU laws, as amended from time to time and as defined in the German Order, set forth in the condition are: CRR articles 99, 394, 430 and Part Six: Title II and Title III; CRR Reporting ITS annexes I, II, III, IV, V, VIII, IX, X, XI, XII and XIII, as applicable.

²² *Id.*

²³ See *Order Specifying the Manner and Format of Filing Unaudited Financial and Operational Information by Security-Based Swap Dealers and Major Security-Based Swap Participants that are not U.S. Persons and are Relying on Substituted Compliance Determinations with Respect to Rule 18a-7*, Exchange Act Release No. 93335 (Oct. 14, 2021), 86 FR 59208 (Oct. 26, 2021).

²⁴ See German Order, 86 FR at 59820.

²⁵ *Id.* Specifically, paragraph (b)(1)(viii) of Rule 18a-6, which is part of the Linked Recordkeeping Requirements.

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approval under CRR Article 9 and related approvals for application of other requirements at this level, MSESE will need approvals from, or must otherwise coordinate with, the European Central Bank (“**ECB**”), the Bundesanstalt für Finanzdienstleistungsaufsicht (“**BaFin**”), and the Deutsche Bundesbank (“**Bundesbank**”). MSESE and similarly situated firms are going through a transition period in which MSESE is first required to be authorized as a CRR credit institution under Article 8 of Directive 2013/36/EU (“**CRD**”) which will on completion lead to a transfer of supervisory responsibility over MSESE from the BaFin to the ECB under the Single Supervisory Mechanism (“**SSM**”). ECB supervision under the SSM is conducted through a Joint Supervisory Team comprising of representatives of the ECB, BaFin, and Bundesbank. This means these authorities will be engaged in preparing for that transition at the same time they are considering MSESE’s request to replace the Article 7 waiver with the alternative approvals under the CRR. The ECB have indicated that the process of considering the alternative approvals required to replace the Article 7 waiver would require a full assessment with a decision to be taken post finalization of the authorization process. Consequently, MSESE is seeking written assurance that the Division staff will not recommend enforcement action to the Commission under the Exchange Act Capital Requirements, Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements if MSESE operates as if it were applying substituted compliance with respect to these requirements until the date that MSESE has taken the necessary steps and obtained the necessary approvals to cease operating pursuant to the Article 7 waiver and, therefore, is able to apply substituted compliance with respect to these requirements pursuant to the terms and conditions of the German Order.

In support of this request, MSESE could meet the following terms and conditions of the German Order for applying substituted compliance with respect to the Exchange Act Capital Requirements: (1) the Recordkeeping/Notification Condition of paragraph (c)(1)(ii) of the German Order; (2) the Net Liquid Assets Test Condition of paragraph (c)(1)(iii)(A)(1) of the German Order; (3) the Quarterly Record Condition of paragraph (c)(1)(iii)(A)(2) of the German Order; and (4) the Notification Condition of paragraph (c)(1)(iii)(A)(3) of the German Order. In addition, MSEHSE (the immediate holding company) could meet the following terms and conditions of the German Order: (1) the Net Liquid Assets Test Condition of paragraph (c)(1)(iii)(A)(1) of the German Order; (2) the Quarterly Record Condition of paragraph (c)(1)(iii)(A)(2) of the German Order; and (3) the Notification Condition of paragraph (c)(1)(iii)(A)(3) of the German Order.

MSESE could meet the terms and conditions for applying substituted compliance with respect to the Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements in paragraphs (f)(1), (f)(2), (f)(3), and (f)(4) of the German Order, other than: (1) the condition that MSESE apply substituted compliance with respect to

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the Exchange Act Capital Requirements; and (2) certain conditions requiring MSESE to be subject to and comply with related German or EU recordkeeping, reporting, or notification requirements that MSEHSE is subject to because of the Article 7 waiver. MSEHSE could meet the conditions.

In further support of the request, MSESE and MSEHSE could file periodic financial and operational information with the Commission pursuant to the terms and conditions of the Manner and Format Order and present that information in accordance with Local GAAP as if they were applying substituted compliance with respect to Rule 18a-7(a)(1).

Finally, MSESE and MSEHSE could provide the Commission with their most recent statements of financial condition filed with German and EU authorities (whether audited or unaudited) and that MSESE could provide the Commission with a written status update at the end of each month on its progress in taking the necessary steps and obtaining the necessary approvals to become eligible to apply substituted compliance with respect to the Exchange Act Capital Requirements, Linked Recordkeeping Requirements, Linked Reporting Requirements, and Linked Notification Requirements pursuant to the terms and conditions of the German Order.

* * * * *

We appreciate the time and consideration shown by the Commission as MSESE takes steps to come into compliance with condition (c)(1) of the German Order.

Please contact us if discussion of this letter would be helpful.

Sincerely,



Jana Waehrisch
Managing Director



Chris Beatty
Managing Director

CC: Michael Macchiaroli, Thomas McGowan, Raymond A. Lombardo, Sheila Swartz, Carol McGee (Commission)

Oliver Behrens, Kim Lazaroo, Anthony Mullineaux, Gareth James, Kate Mozzicarelli, Eva Mund, Andrew Nash, Maria-Ines Rajj, Yujing Yue, Andrew Lipton (MS)