January 25, 2021

Vanessa A. Countryman
Secretary
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Re: Notice of Substituted Compliance Application Submitted by the French Autorité des Marchés Financiers and the Autorité de Contrôle Prudential et de Résolution in Connection With Certain Requirements Applicable to Non-U.S. Security-Based Swap Entities Subject to Regulation in the French Republic; Proposed Order (File No. S7-22-20)

Dear Ms. Countryman:

The Securities and Financial Markets Association ("**SIFMA**")[1] appreciates the opportunity to comment on the above-captioned notice by the Securities and Exchange Commission ("**SEC**" or "**Commission**") regarding the substituted compliance application submitted by the French Autorité des Marchés Financiers ("**AMF**") and the Autorité de Contrôle Prudential et de Résolution ("**ACPR**") in connection with certain requirements applicable to security-based swap ("**SBS**") dealers ("**SBSDs**") and major SBS participants (together with SBSDs, "**SBS Entities**") subject to regulation in the French Republic, and the proposed order (the "**French Order**") providing for the conditional substituted compliance in connection with the application (together, the "**Proposal**").[2]

In many respects, the Proposal reflects a thoughtful, holistic approach to substituted compliance. However, the Proposal still includes certain conditions and limitations that raise significant issues, as discussed below.

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[1] SIFMA is the leading trade association for broker-dealers, investment banks and asset managers operating in the U.S. and global capital markets. On behalf of our industry, nearly 1 million employees, we advocate for legislation, regulation and business policy, affecting retail and institutional investors, equity and fixed income markets and related products and services. We serve as an industry-coordinating body to promote fair and orderly markets, informed regulatory compliance, and efficient market operations and resiliency. We also provide a forum for industry policy and professional development. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA).

[2] Securities Exchange Act of 1934 ("**Exchange Act**") Release No. 34-90766 (Dec. 22, 2020), 85 Fed. Reg. 85720 (Dec. 29, 2020).

I. Scope of Foreign Requirements Identified as Conditions to Substituted Compliance

The application by the AMF and ACPR identified a wide range of European Union ("**EU**") and French requirements potentially relevant to the Commission's substituted compliance analysis, including in some instances requirements that have no analogue among relevant Exchange Act requirements. The French Order generally identifies the full range of these requirements as conditions to substituted compliance. In other words, the French Order would require an SBS Entity relying on substituted compliance to be subject to, and comply with, a broader range of substantive requirements under EU and French laws than would be the case if the SBS Entity simply complied directly with the relevant Exchange Act requirements. The Commission's Final Order Granting Conditional Substituted Compliance in Connection With Certain Requirements Applicable to SBS Entities Subject to Regulation in the Federal Republic of Germany (the "**German Order**" and, together with the French Order, the "**Orders**")[3] generally takes the same approach.

For the following reasons, this approach will result in undue burdens and issues for French and German SBS Entities:

- With respect to certain Exchange Act requirements that will apply to an SBS Entity on an entity-wide basis (including all its branches), the Orders cite in their conditions a mix of EU and French or German requirements that vary as to their territorial scope. Some of those requirements similarly apply to a French or German SBS Entity on an entity-wide basis (including all its branches), but others do not apply to the SBS activities of a third-country branch of such an SBS Entity. Because the Orders also require that an SBS Entity relying on substituted compliance be subject to, and comply with, *all* of the referenced EU and French or German requirements, the effect of referencing this mix of requirements will be to prevent an SBS Entity from relying on substituted compliance in its third-country branches.[4] In our view, this is an unnecessary result in situations where the cited entity-wide EU and French or German requirements are sufficient, standing alone, to produce comparable regulatory outcomes to the relevant Exchange Act requirement. In these situations, the Commission should eliminate references to the EU and French or German requirements that do not apply to third-country branches. Not only is the result unnecessary, but it would

[3] *See* Order Granting Conditional Substituted Compliance in Connection With Certain Requirements Applicable to Non-U.S. [SBS Entities] Subject to Regulation in the Federal Republic of Germany, 85 Fed. Reg. 85686 (Dec. 29, 2020).

[4] *See* Proposal at 85723 ("[T]he proposed Order would not provide substituted compliance when an SBS Entity is excused from compliance with relevant foreign provisions, such as, for example, if relevant member French or EU requirements do not apply to the [SBS] activities of a third-country branch of a French SBS Entity."); *see also* German Order at 85688, n. 12.

undermine one of the key goals of substituted compliance, which is to allow SBS Entities to apply consistent, global compliance policies, procedures, and systems.

- The Orders would require that, if responsibility for ensuring compliance with any provision of Markets in Financial Instruments Directive 2014/65/EU ("**MiFID**") or any other EU or French or German requirement adopted pursuant to MiFID listed in the Orders as a condition to substituted compliance is allocated to an authority of the Member State of the EU in whose territory a French or German SBS Entity provides a service, the AMF/ACPR or Bundesanstalt für Finanzdienstleistungsaufsicht ("**BaFin**"), respectively, must be the authority responsible for supervision and enforcement of that provision or requirement in relation to the particular service. Similarly, the Orders would require that, if responsibility for ensuring compliance with any provision of the Market Abuse Regulation (EU) 596/2014 ("**MAR**") or any other EU requirement adopted pursuant to MAR listed in the Orders as a condition to substituted compliance is allocated to one or more authorities of a Member State of the EU, one of such authorities must be the AMF/ACPR or BaFin. Although we understand that the Commission has included these conditions in order to ensure that the prerequisites with respect to supervision and enforcement are satisfied, we are concerned that they will in practice lead to an untenable patchwork of substituted compliance because, as the Commission noted in the Orders, compliance with certain MiFID requirements is supervised by the regulator in the jurisdiction where the services are provided.[5]

  Specifically, a French or German SBS Entity operating branches throughout the EU would be subject to supervision by the AMF or BaFin, respectively, with respect to its home office's compliance with certain MiFID requirements. However, the SBS Entity's other EU branches would be subject to supervision with respect to the same requirements by the regulator in the EU Member State in which such branch was operating. Consequently, the SBS Entity could not avail itself of substituted compliance unless authorities or regulated SBS Entities in every or nearly every one of the 27 EU Member States submit their own substituted compliance applications covering local branches of SBS Entities, and the Commission reviews and responds to those applications and enters into memoranda of understanding ("**MoUs**") with authorities in each of these Member States. For example, a French SBS Entity operating branches and/or providing services throughout the EU could rely on the French Order to substitute compliance with EU and French trading relationship documentation requirements where it provides a service in France, but would need to apply the Commission's trading relationship documentation requirements to services provided in the 26 other EU Member States.

[5] *See* Proposal at 85724; German Order at 85689.

Again, in our view this result is unnecessary in situations where there are other EU and French or German requirements that are not subject to this MiFID jurisdictional allocation and are sufficient, standing alone, to produce comparable regulatory outcomes to the relevant Exchange Act requirement. In these situations, the Commission should eliminate references to the MiFID requirements subject to this jurisdictional allocation.[6]

- Where one of the Orders makes compliance with a specific EU, French, or German requirement a condition to substituted compliance, it is imposing on a French or German SBS Entity additional burdens and risks beyond those already present by virtue of the SBS Entity being subject to EU and French or German law. Specifically, the SBS Entity would need to apply its SBS governance framework, including the senior officer certification required to accompany its registration form,[7] to that EU, French, or German requirement. In addition, non-compliance with that EU, French, or German requirement would subject the SBS Entity to potential liability for non-compliance with the Exchange Act.[8] If, however, that EU, French, or German requirement is superfluous to the Commission's comparability analysis—*i.e.*, where other EU, French, or German requirements are sufficient, standing alone, to produce comparable regulatory outcomes to the relevant Exchange Act requirement—the effect of including that superfluous EU, French, or German requirement within the Order's conditions is to expand the required scope of SBS governance requirements and potential U.S. liability beyond what would apply if the SBS Entity did not rely on substituted compliance.

To address these burdens and issues, we recommend that the Commission make the following modifications to the Orders:

- **Internal Risk Management.** In the area of internal risk management, Exchange Act Section 15F(j)(2) and related aspects of Exchange Act Rule 15Fh-3(h)(2)(iii)(I) solely require an SBS Entity to establish robust and professional risk management systems adequate for managing its day-to-day business (as well as related policies and procedures). In contrast, the Orders would require French and German SBS Entities to comply with an expansive range of detailed and

[6] The Commission also requested comment on whether it should allow (i) German branches of French SBS Entities to use substituted compliance in circumstances where responsibility for ensuring compliance with any provision of MiFID, MAR, or any other EU requirement adopted pursuant to MiFID or MAR is allocated to BaFin and (ii) French branches of German SBS Entities to use substituted compliance in circumstances where such responsibility is allocated to the AMF or ACPR. Proposal at 85736. We think that allowing such use of substituted compliance would be appropriate, considering that the Commission has reviewed the supervision and enforcement frameworks of each of BaFin and the AMF and ACPR. However, it would not suffice to address the issue described above.

[7] *See* Form SBSE-C (requiring a senior officer to certify that he or she has reasonably determined that the SBS Entity has developed and implemented written policies and procedures reasonably designed to prevent violation of federal securities laws and the rules thereunder).

[8] *See* also discussion in Section III below.

prescriptive requirements under Directive 2013/36/EU ("**CRD**") (together with implementing French or German laws) that go beyond this high-level Exchange Act requirement.[9] They also would require such SBS Entities to comply with Commission Delegated Regulation (EU) 2017/565 ("**MiFID Org Reg**") Article 22, which relates to the compliance function, not risk management. The Commission should eliminate these references, instead only citing MiFID Articles 16(4) and 16(5) (including French or German implementing laws therefor), MiFID Org Reg Articles 21, 23, and 24, and Commission Delegated Regulation (EU) 2016/2251 ("**EMIR Margin RTS**") Article 2.

- **Trade Acknowledgment and Verification.** The Commission should eliminate the references to MiFID provisions in connection with trade acknowledgment and verification requirements, instead relying solely on European Market Infrastructure Regulation (EU) 648/2012 ("**EMIR**") for comparability. This change would address the issues noted above because, unlike MiFID Article 25(6), EMIR Article 11(1)(a) and Commission Delegated Regulation (EU) 149/2013 ("**EMIR RTS**") Article 12 apply on an entity-wide basis,[10] with responsibility for supervision and enforcement also allocated on an entity-wide basis to the AMF (for French SBS Entities) or BaFin (for German SBS Entities). Although we recognize that, in the German Order, the Commission concluded that both EMIR and MiFID requirements contribute to the conclusion that German and EU law produces a comparable regulatory outcome to the Exchange Act trade acknowledgment and verification requirements, we respectfully submit that EMIR's confirmation requirements, standing alone, are sufficient to produce comparable regulatory outcomes, given that those requirements are essentially identical to the Commodity Futures Trading Commission's ("**CFTC**") confirmation rule and the Commission's trade acknowledgment and verification

[9] We note that the applications by the AMF/ACPR and BaFin address these CRD requirements in connection with internal risk management because the relevant sections of those applications were analyzing comparability with Exchange Act Rule 18a-1(f), not Section 15F(j)(2) or Rule 15Fh-3(h)(2)(iii)(I). The Commission has elected to address Rule 18a-1(f) separately in connection with substituted compliance for capital requirements applicable to non-prudentially regulated SBS Entities. Therefore to the extent the Commission considers these CRD requirements to be relevant to its comparability analysis for Rule 18a-1(f), it should identify them as conditions to substituted compliance with Rule 18a-1, not Section 15F(j)(2) or Rule 15Fh-3(h)(2)(iii)(I).

[10] We note in this regard that these EMIR provisions apply to a French or German SBS Entity when they transact with a third-country (*i.e.*, non-EU) counterparty, including a U.S. counterparty. *See* European Securities and Markets Authority Questions and Answers on Implementation of EMIR, OTC Question 12, *available at* https://www.esma.europa.eu/sites/default/files/library/esma70-1861941480-52_qa_on_emir_implementation.pdf ("Article 11 of EMIR, which provides the basis of these requirements, applies wherever at least one counterparty is established within the EU. Therefore, where an EU counterparty is transacting with a third country entity, the EU counterparty would be required to ensure that the requirements for portfolio reconciliation, dispute resolution, timely confirmation and portfolio compression are met for the relevant portfolio and/or transactions even though the third country entity would not itself be subject to EMIR. However, if the third country entity is established in a jurisdiction for which the Commission has adopted an implementing act under Article 13 of EMIR, the counterparties could comply with equivalent rules in the third country.").

requirements are closely aligned with that CFTC confirmation rule.[11] In light of this, conditioning substituted compliance on compliance with MiFID requirements is unnecessary, and at the same time, undermines in effect the availability of substituted compliance.

- **Trading Relationship Documentation.** For trading relationship documentation, where a French or German SBS Entity is subject to the documentation requirements set forth in EMIR Margin RTS Article 2 (*e.g.*, for SBS with a financial counterparty), the Commission should permit an SBS Entity to avail itself of substituted compliance, even if the SBS Entity is not subject to MiFID Article 25(5) or if responsibility for supervision and enforcement of MiFID Article 25(5) is not allocated to the AMF or BaFin. Because EMIR Margin RTS Article 2 imposes substantially similar requirements as SEC Rule 15Fi-5 (other than paragraph (b)(5)), and it applies on an entity-wide basis,[12] this modified approach would still produce comparable regulatory outcomes.[13]

- **Internal Supervision and Compliance.** The Orders' conditions for substituted compliance in connection with Exchange Act Rule 15Fh-3(h), Exchange Act Sections 15F(j)(4)(A) and (j)(5), Exchange Act Section 15F(k), and Exchange Act Rule 15Fk-1 include several provisions of MiFID and CRD that are not necessary to justify substituted compliance, namely MiFID Org Reg Articles 72-76 and Annex IV (*various record-keeping obligations*) and CRD Articles 79 to 87

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[11] SEC Rule 15Fi-2 provides that a trade acknowledgment disclosing all the terms of an uncleared SBS transaction must be promptly provided through electronic means. Similarly, pursuant to Article 12 of EMIR RTS and Article 11(1)(a) of EMIR, a confirmation disclosing the terms of an uncleared over-the-counter ("**OTC**") derivative contract must be provided as soon as possible through electronic means. SEC Rule 15Fi-2(d) also provides that an SBS Entity "must establish, maintain, and enforce written policies and procedures that are reasonably designed to obtain prompt verification of the terms of the trade acknowledgment" and "promptly verify the accuracy of, or dispute with its counterparty, the terms of the trade acknowledgment." Article 11(1) of EMIR likewise provides that an SBS Entity must have in place "appropriate procedures and arrangements . . . to measure, monitor and mitigate operational risk and counterparty credit risk, including at least: . . . formalised processes which are robust, resilient and auditable in order to reconcile portfolios, to manage the associated risk and to identify disputes between parties early and resolve them, and to monitor the value of outstanding contracts."

[12] We note in this regard that the EMIR Margin RTS include specific provisions addressing their application to non-centrally cleared OTC derivatives with a third-country (*i.e.*, non-EU) counterparty, thus confirming that a French or German SBS Entity is subject to the EMIR Margin RTS when transacting with such a counterparty. *See* Articles 24 and 26 of the EMIR Margin RTS.

[13] SEC Rule 15Fi-5(a)(2) requires an SBS Entity to establish, maintain, and follow written policies and procedures that are approved in writing by a senior officer and "reasonably designed to ensure that the [SBS Entity] . . . executes written [SBS] trading relationship documentation with its counterparty." The SBS trading relationship documentation must be in writing and include all terms governing the trading relationship, including the process for determining the value of each SBS.

Article 2 of the EMIR Margin RTS similarly requires an SBS Entity to establish, apply, and document certain risk management procedures with respect to uncleared OTC derivatives contracts. These risk management procedures, like the SBS trading relationship documentation under SEC Rule 15Fi-5, require inclusion of the terms of all necessary agreements entered into by counterparties, including all calculation methods used in relation to payment obligations.

(*treatment of risk*) (and French or German implementing laws therefor). The Commission should eliminate the references to these provisions in these conditions.[14]

- **Recordkeeping, Reporting, Notification, and Securities Counts.** The French Order would require both prudentially regulated and non-prudentially regulated SBS Entities to comply with specific EU and French laws in order to avail themselves of substituted compliance for recordkeeping, reporting, notification, and securities count requirements. Many of the EU laws were not included in the German Order as a condition for substituted compliance for those requirements. Additionally, many of the French laws have no comparable German law reference in the German Order.

  For example, to avail itself of substituted compliance with respect to the reporting requirements of Exchange Act Rule 18a-7, the French Order would require an SBS Entity to comply with, among other provisions, Capital Requirements Regulation (EU) No 575/2013 ("**CRR**") Articles 26(2), 132(5), 154, 191, 321, 325bi, 350, 368, and 431-455; CRD Article 89; MiFID Article 16(8)-(10); MiFID Delegated Directive Articles 2, 8, 72(2), and Annex I; Code monétaire et financier ("**MFC**") Articles L. 511-45 and L. 533-10; Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 Article 34; Decree of 6 September 2017 Articles 3 and 10; French Commerce Code Articles L. 232-1, R. 232-1 through R. 232-8, and L. 823-1 through L. 823-8-1; and AMF General Regulation Articles 312-6 and 312-7.[15] However, the German Order does not require an SBS Entity to comply with any of these EU laws or comparable German implementing laws to rely on substituted compliance with respect to the same reporting requirements under Exchange Act Rule 18a-7.[16]

  We understand that some of these references to EU and French law are intended to relate to Commission regulations that apply only to non-prudentially regulated SBS Entities, such as certain provisions of Exchange Act Rules 18a-7 and 18a-8. However, conditioning substituted compliance for French SBS Entities on laws that German SBS Entities are not required to comply with to avail themselves of substituted compliance would create unwarranted disparities between SBS Entities in different EU jurisdictions. Specifically, French SBS Entities would be subject to more extensive SBS governance requirements, exposing them to greater

[14] As a corollary point, the conditions to the Orders should not impose obligations that go beyond the Exchange Act requirements addressed by the Orders. For example, the Orders would require that an SBS Entity's annual compliance report include a certification that "under penalty of law, the report is accurate and complete." To be consistent with the linked Exchange Act requirement, Rule 15Fk-1(c)(2)(ii)(D), the condition should instead be rephrased to require a certification that to the best of the certifier's knowledge and reasonable belief and under penalty of law, the information contained in the compliance report is accurate and complete in all material respects (*i.e.,* it should contain knowledge and materiality qualifiers, like Rule 15Fk-1(c)(2)(ii)(D)).

[15] French Order at (f)(3).

[16] German Order at (e)(3).

potential U.S. liability. For this reason, the Commission should distinguish between the EU and French laws that are conditions to substituted compliance for non-prudentially regulated SBS Entities versus prudentially regulated SBS Entities. For prudentially regulated SBS Entities the range of EU laws included as conditions to substituted compliance for French SBS Entities should be limited to the same EU laws included as conditions to substituted compliance in the German Order. Finally, there should be no reason to condition substituted compliance for French SBS Entities on French implementing laws where the German Order does not cite any German implementing laws; in these areas, the French Order should only reference EU laws that do not require national implementation.

In addition, because this section of the French Order does not distinguish between prudentially regulated and non-prudentially regulated SBS Entities, it could be read to require French non-prudentially regulated SBS Entities to comply with EU and French requirements that apply only to prudentially regulated entities in France. By clarifying which conditions to substituted compliance apply to prudentially regulated versus non-prudentially regulated SBS Entities, the Commission would clarify this issue.

II. Scope of Reliance on Substituted Compliance[17]

There may be certain instances where an SBS Entity is not subject to the EU and French requirements identified as conditions to substituted compliance, such as due to the cross-border issues noted in Section I of this letter. SBS Entities may also conclude that, for operational reasons,[18] they prefer to comply directly with certain Exchange Act requirements (*i.e.*, not to rely on substituted compliance with those requirements). We would envision therefore that when providing notice to the Commission pursuant to condition (7) of the French Order (condition (6) of the German Order) that the SBS Entity is relying on substituted compliance, the SBS Entity could identify the particular Exchange Act requirements for which it is so relying. In so doing, the SBS Entity could identify a narrower range of Exchange Act requirements than those for which substituted compliance is theoretically available, *i.e.*, it could elect to rely on substituted compliance for a subset of the Exchange Act requirements identified by the relevant Order.[19] We request that the Commission confirm our understanding.

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[17] These comments apply equally to the German Order.

[18] An example could include a group that has multiple affiliated SBS Entity registrants, including U.S. registrants, and that elects to adopt a consistent group-wide compliance program. Another example could include a non-U.S. registrant that cannot rely on substituted compliance in certain branches due to the cross-border issues noted above, and accordingly, elects to comply with relevant Exchange Act requirements directly across all its branches, even those that could rely on substituted compliance.

[19] By way of example, the French Order would condition substituted compliance in connection with requirements to make and keep current certain records on compliance with, among other EU and French requirements, MiFID Articles 25(1), 25(3), 24(5), and 25(6), MiFID Org Reg Articles 59 (which relates to MiFID Article 25(6)) and 73 (which related to MiFID Article 25(5)) and related aspects of Annex I and Annex IV, and MFC Article L. 533-13, L. 533-14, 533-15 (which implement the aforementioned MiFID provisions). The French Order would condition

III. Supervision and Enforcement of EU and French Laws[20]

The Proposal states that when an SBS Entity seeks to rely on substituted compliance, non-compliance with the applicable French and EU requirements would lead to a violation of the Commission's requirements and potential enforcement action by the Commission.[21] The Commission should clarify that an SBS Entity would not violate the Commission's requirements where the relevant foreign regulatory authority has found no violation of the comparable French or EU requirement and the SBS Entity's conduct would have complied with the Commission's requirements (even if the SBS Entity relied on French and EU rules that imposed stricter or additional requirements). On the other hand, if a foreign regulatory authority finds that an SBS Entity has violated a foreign requirement, the SBS Entity was relying on substituted compliance with that requirement, and the SBS Entity's conduct would not have complied with the Commission's requirements, the Commission could take appropriate enforcement or disciplinary action. We believe that this understanding is consistent with the meaning of "*substituted* compliance," inasmuch as it would avoid subjecting the SBS Entity to greater potential liability than if it complied directly with the Exchange Act requirements for which it is substituting compliance. The clarification is particularly necessary due to the significantly broader substantive scope of EU and EU Member State requirements, which extend beyond SBS, and the approach in the Orders to cite to a greater number of EU and EU Member State requirements as conditions to the availability of substituted compliance.[22]

The Commission should also clarify that it will not independently examine for or otherwise assess whether an SBS Entity is complying with EU or French requirements, but rather

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substituted compliance in connection with requirements to preserve records on compliance with, among other EU and French requirements, MiFID Articles 25(5) and 25(6), MiFID Org Reg Articles 59 and 73, and MFC Articles L. 533-14 and L. 533-15. Instead of relying on substituted compliance by complying with these MiFID requirements, an SBS Entity should be permitted to comply directly with Exchange Act Rules 18a-5(a)(6)/(b)(6) (trade confirmation records), 18a-5(a)(7)/(b)(7) (counterparty information records), 18a-6(b)(1)(vi)/(b)(2)(iii) (account documents), and 18a-6(b)(1)(vii)/(b)(2)(iv) (written agreements)—which are the Exchange Act requirements to which the aforementioned MiFID requirements relate—even as the SBS Entity relies on substituted compliance with respect to other aspects of Rules 18a-5 and 18a-6.

[20] These comments apply equally to the German Order.

[21] Proposal at 85722.

[22] Even assuming that the Commission makes the edits to the Orders recommended in Section I, this would still be the case as illustrated, for example, in the areas of record creation and financial reporting. In the area of record creation, it should be possible for an SBS Entity to demonstrate compliance, if when facing a request by the Commission staff for a specific record mandated under Commission regulations, it produces an equivalent record, such record is required of it under the cited EU or home country laws, and the SBS Entity is subject to home country supervision in that regard. The Commission has chosen to cite both specific and general provisions on record creation, such that, absent such clarification, there would be significant doubt as to what the Commission might do when enforcing on foreign laws even if presented with equivalent records to what it would require under its own rules.

This is even more clear in the area of financial reporting. In addition to citing to a multitude of home country requirements (and indeed many more under the French Order than the German Order, see Section I above), the Commission has made clear that it will require some form of FOCUS reporting from SBS Entities relying on substituted compliance in that regard (see also Section VIII below). As SBS Entities will provide, via the Financial Industry Regulatory Authority's portal, FOCUS reports to the Commission, executed by the principal executive

it will look to the relevant foreign regulatory authority to conduct those examinations and make those assessments. Of course, if the Commission suspects a violation of a foreign requirement, it can and should consult with the relevant foreign regulatory authority, for example through an MoU with that authority. This approach is consistent with the fact that, in making its substituted compliance determination, the Commission has taken into account the ability of the relevant foreign regulatory authority to supervise and enforce compliance with the relevant foreign jurisdiction's standards.[23] Accordingly, the Commission should have confidence, when it has made a comparability determination, that the relevant foreign regulatory authority is up to the task of supervision and enforcement. Further, if the Commission instead independently supervised and enforced compliance with foreign laws, doing so would undo the very benefits of regulatory efficiency and international comity that are the goals of substituted compliance. Finally, as a practical matter, the Commission lacks the expertise to interpret and apply foreign laws (just as foreign regulators are in no position to interpret and apply U.S. laws).

IV. Transition Period[24]

The manner in which the Orders approach substituted compliance for certain entity-level Commission requirements under the Exchange Act, including the Orders' conditions, could result in such requirements still applying to a non-U.S. SBS Entity's SBS with non-U.S. persons and require written agreement by the counterparty, such as under trading relationship documentation requirements. Given that potential registrants are learning what the scope of these requirements will be only just now as part of the Commission's implementation of its substituted compliance framework, there may not be sufficient time to obtain these written agreements from non-U.S. counterparties prior to the November 1, 2021 date by which SBSDs must register with the Commission. To account for this issue, we request that the Commission provide an additional transition period of one year for a non-U.S. SBS Entity to come into compliance with any documentation requirements that will apply to the SBS Entity's existing non-U.S. counterparties as of the date of the SBS Entity's registration.

V. Capital Requirements for SBS Entities With No Prudential Regulator

We support the proposal to grant substituted compliance in connection with capital requirements for non-prudentially regulated SBS Entities without imposing additional conditions. This approach is appropriate given the comprehensiveness of capital and liquidity requirements in France and the EU as well as the different regulatory and insolvency framework that applies to the EU non-prudentially regulated SBS Entities that would be relying on this substituted compliance determination. Such entities are primarily engaged in investment

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officer, principal financial officer, and principal operations officer, or equivalent, under penalty of federal criminal statutes in case of intentional misstatements or omissions, the Commission will be in possession of a U.S.-law backed enforcement mechanism. This being the case, it would seem strained for the Commission to bring an enforcement action for non-compliance with foreign financial reporting rules where such non-compliance has no impact on the statements or completeness of the FOCUS reports so furnished.

[23] Proposal at 85721.

[24] These comments apply equally to the German Order.

services, including sales and trading, capital markets services, and settlement and clearing services, not lending business, but nonetheless are subject to the same prudential and insolvency frameworks as deposit-taking institutions, and will have access to Eurosystem standing credit facilities (similar to the Federal Reserve discount window), as described in further detail below.

Additionally, imposing multiple, overlapping, and different capital and liquidity requirements on SBS Entities without a prudential regulator would be inconsistent with such entities' prudent risk management because these SBS Entities would be subject to inconsistent standards with respect to managing their capital and liquidity, which in turn determine how they manage risk. Consequently, the imposition of additional conditions is neither necessary nor appropriate.

a. Additional Conditions for Substituted Compliance in Connection with Capital Requirements

We understand that the Commission is considering imposing certain conditions to substituted compliance with respect to capital requirements. We are concerned that some of these conditions would be particularly burdensome to, or inappropriate for, SBS Entities that do not have a prudential regulator. In particular, requiring a non-prudentially regulated SBS Entity to maintain a minimum amount of liquid assets, such as a minimum ratio of liquid assets to illiquid assets, or subjecting a non-prudentially regulated SBS Entity to a specific liquidity requirement,[25] would impose unnecessary burdens on such entities.

The Commission should not include these conditions because they would be duplicative of, and (depending on their design) inconsistent with, EU and French requirements that are applicable to non-prudentially regulated SBS Entities. Such SBS Entities are already subject to EU and French liquidity requirements that are designed to address these matters. Specifically, EU requirements address liquidity risk by imposing separate liquidity requirements composed of three main obligations, which the Commission already has included as conditions to substituted compliance with respect to capital requirements:[26]

- the Liquidity Coverage Ratio, which requires an EU SBS Entity to hold an amount of sufficiently liquid assets to meet its expected payment obligations under gravely stressed conditions for thirty days;[27]

[25] Proposal at 85737.

[26] French Order at (c)(1).

[27] CRR, Article 412(1).

- the Net Stable Funding Ratio ("**NSFR**"), which requires an EU SBS Entity to hold a diversity of stable funding instruments sufficient to meet long term obligations under both normal and stressed conditions;[28] and

- the internal liquidity adequacy assessment process, which requires an EU SBS Entity to maintain robust strategies, policies, processes, and systems for the identification, measurement, management, and monitoring of liquidity risk over an appropriate set of time horizons, including intra-day, and management and monitoring of funding positions.[29]

EU SBS Entities also are subject to bank-style resolution regimes under the Bank Recovery and Resolution Directive, which makes their liquidity risks less significant than standalone U.S. SBS Entities. The existence of resolution powers permits the relevant resolution authorities to take action well in advance of resolution in order to preserve the continuity of critical services and reduce the impact of an entity's failure on financial stability, including through the orderly winding down of activities or restructuring supported by the entity's own funds. Accordingly, unlike the U.S. Bankruptcy Code, the focus of the EU resolution regime is not the liquidation of the institution.

Unlike U.S. SBS Entities that do not have a prudential regulator, certain EU SBS Entities will have access to short-term liquidity through relevant EU Member State central banks. For example, staring June 26, 2021, large investment firms with €30 billion in assets and above that engage in dealing on own account will be required to be re-authorized by the European Central Bank ("**ECB**") as credit institutions, which will grant them access to Eurosystem standing facilities.[30]

In addition to being duplicative, imposing a minimum ratio of liquid assets to illiquid assets would create additional unjustifiable burdens. The Commission would have to define "liquid" versus "illiquid" assets in order to operationalize such a condition. However, since the Commission did not propose definitions in the French Order, absent some additional comment period, any definitions in the final French Order would be adopted without the benefit of public input. Moreover, requiring this minimum ratio would be similar to the Commission subjecting EU non-prudentially regulated SBS Entities to a net liquid assets test, even though EU policymakers have determined instead to apply a risk-based approach to capital requirements.

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[28] CRR, Article 413(1) As of June 28, 2021, the Basel III NSFR requirements will become applicable, as specified in CRR, Articles 428a to 428az introduced by Capital Requirements Regulation II (2019/876) ("**CRR II**"), Article 1(116).

[29] Capital Requirements Directive (2013/36/EU) ("**CRD IV**"), Article 86, implemented into French law by Article L. 511-41-1 B and L. 511-41-1 C for credit institutions and Article L. 533-2-2 and L. 533-2-3 for investment firms, as well as Articles 148 to 186 of the *Arrêté* of 3 November 2014 on internal control and Article 7 of the *Arrêté* of 3 November 2014 relating to the process of prudential supervision and risk assessment of banking service providers and investment firms.

[30] *See* Investment Firms Directive (2019/2034/EU), Recital 7. National central banks may also allow investment firms to make use of intraday credit under TARGET2. *See* TARGET Guideline (EU/2012/27), Annex III, L 30/67, available at https://www.ecb.europa.eu/ecb/legal/pdf/l_03020130130en00010093.pdf.

Such an imposition would change the way these entities conduct business in a way that may be inconsistent with the requirements of their home country regulators.

At most the Commission should condition its substituted compliance determination with respect to its capital requirements on a non-prudentially regulated SBS Entity's compliance with the relevant EU and French capital and liquidity requirements, as it has done in the Proposal.[31] The Commission should not, however, impose its own net capital requirements and liquidity standards on SBS Entities.

b. Amendments to CRR and CRD

The Commission's French Order should not be impacted by the amendments to EU and French capital requirements brought about by the Capital Requirements Directive V (2019/878/EU) ("**CRD V**") or CRR II, or additional amendments over time, because these amendments do not impact the comparability analysis the Commission set forth in the Proposal.

CRD IV and CRR were amended on May 20, 2019 by CRD V and CRR II, which further implement Basel III standards. CRD V has been implemented in France by a series of legislative and regulatory texts that were published in late December 2020. CRR II is directly applicable in France since its entry into force in June 2019, but part of its provisions will become applicable in the course of 2021. In the Annex attached to this letter, we have included a summary of relevant prudential and related requirements introduced or amended by the French implementation texts of CRD V and by the provisions of CRR II that will become applicable in 2021 or later. These changes enhance the prudential requirements applicable to French SBS Entities and should therefore only have a positive bearing on the assessment of comparability with the Commission's rules.

VI. Margin Requirements for SBS Entities With No Prudential Regulator

We support the Commission's decision to grant substituted compliance in connection with margin requirements for non-prudentially regulated SBS Entities without imposing additional conditions. As the Commission correctly concluded, EU margin requirements are comparable to the Exchange Act margin requirements for non-prudentially regulated SBS Entities. The Commission modified its proposed margin regulations for non-prudentially regulated SBS Entities to align the final rule more closely with the margin rules of the CFTC and U.S. prudential regulators, and consequently, with the Basel Committee on Banking Supervision ("**BCBS**") and the Board of International Organizations of Securities Commissions ("**IOSCO**") Global Standards on Margin.[32] EU margin requirements are similarly based on the BCBS-IOSCO Global Standards on Margin. EU margin requirements produce analogous regulatory outcomes to those associated with the Exchange Act margin requirements because the

[31] *See* French Order at (c)(1) (stating that to qualify for substituted compliance with respect to the Commission's capital requirements, a non-prudentially regulated SBS Entity must comply with the capital requirements of the CRR, including Articles 92 and 412).

[32] *See* Capital, Margin, and Segregation Requirements for [SBS Entities] and Capital and Segregation Requirements for Broker-Dealers Capital and Margin Adopting Release, 84 Fed. Reg. 43872, 43908-43909.

requirements subject EU SBS Entities "to financial responsibility practices that are appropriate to the risks associated with their [SBS] businesses."[33]

VII. Recordkeeping, Reporting, and Notification—English Translations

Subject to certain conditions, the French Order would permit substituted compliance in connection with recordkeeping, reporting, and notification requirements for SBS Entities. The Commission requested comment on whether the French Order should be conditioned on an SBS Entity "furnishing to a representative of the Commission upon request an English translation of any record, report, or notification of the SBS Entity that is required to be made, preserved, filed, or subject to examination pursuant to Exchange Act section 15F or the French substituted compliance order."[34]

If the Commission adopts such a condition in the final French Order, we request that the Commission confirm that it will work with an SBS Entity, upon making a request for English translations, to allow for a reasonable time for the requested translations to be made. The time period to furnish such English translations should be commensurate to the scope of the Commission's request.

VIII. Condition Requiring the Filing of Financial and Operational Information in the Manner and Format Required by SEC Rule or Order

SEC Rule 18a-7 requires non-prudentially regulated SBS Entities, on a monthly basis, and prudentially regulated SBS Entities, on a quarterly basis, to file an unaudited financial and operational report known as FOCUS Report Part II ("**Part II**") and FOCUS Report Part IIC ("**Part IIC**"), respectively.

The Proposal would grant SBS Entities substituted compliance with the reporting requirements of SEC Rule 18a-7, but subject to the condition that the SBS Entity file financial and operational information with the Commission or its designee in the manner and format required by Commission rule or order. The Proposal included this condition in order to facilitate cross-firm analysis and monitoring of all registered SBS Entities.[35] The Proposal further contemplates that the Commission might, pursuant to this condition, require non-prudentially regulated French SBS Entities to file financial and operational information with the Financial Industry Regulatory Authority using Part II and prudentially regulated French SBS Entities to do so using Part IIC. However, the Commission would permit the information input into the form to be the same information that the SBS Entity reports to the AMF, ACPR, or other relevant supervisors, with the information presented in accordance with generally accepted accounting principles ("**GAAP**") that the SBS Entity uses to prepare general purpose financial statements in its home jurisdiction instead of U.S. GAAP if other GAAP, such as International Financial

[33] Proposal at 85726.

[34] *Id.* at 85375.

[35] *Id.* at 85733.

Reporting Standards or French GAAP, is used by the SBS Entity in preparing general purpose financial statements.[36]

We support the Commission's view that objectives meant to be advanced by filing information using Part II (for non-prudentially regulated SBS Entities) and Part IIC (for prudentially regulated SBS Entities) can be achieved by these flexible means. Preparing financial information in full conformance with Part II and Part IIC, especially if that information must be presented in accordance with U.S. GAAP, would require affected non-U.S. SBS Entities to engage in significant systems builds, at great expense and with limited benefit to the Commission. In this spirit, we make the following observations and recommendations:

- As we set forth in our letter regarding the Commission's proposed order providing for conditional substituted compliance in connection with the application submitted by BaFin,[37] with respect to prudentially regulated SBS Entities, the Commission should (i) consider providing such entities with the option to fulfill their Rule 18a-7 financial reporting requirements using Commission or the Board of Governors of the Federal Reserve System ("**FRB**") filings in lieu of or in combination with extracts from filings made with home country supervisors; (ii) allow such entities to submit their Part IIC reports at the same consolidation level that is used in the relevant Commission, FRB, or home jurisdiction reports; (iii) permit a non-U.S., prudentially regulated SBS Entity to satisfy information regarding amounts of capital and capital ratio information required by Part IIC in a manner consistent with its home country capital standards and related reporting; and (iv) provide additional time beyond the 30 days for filing Part IIC information and for a year-end filing. These comments apply equally to prudentially regulated SBS Entities in France and Germany.

- In addition, with respect to non-prudentially regulated SBS Entities:

    - Part II includes information relating to a non-prudentially regulated SBS Entity's computations with respect to its required capital and whether certain balance sheet assets are allowable or non-allowable under the Commission's net capital rules. However, given that the Commission has proposed to grant substituted compliance with respect to its capital requirements, this information is not relevant for these entities. Accordingly, the Commission should permit a non-U.S. SBS Entity to satisfy these aspects of Part II by instead submitting computations in a manner consistent with its home country capital standards and related reporting rules.

    - A non-prudentially regulated SBS Entity would be required to submit Part II on a monthly basis. Home country regulators require reports containing

[36] *See id.*

[37] *See* Letter from Kyle Brandon, Managing Director, Head of Derivatives Policy, SIFMA at p. 7-8 (Dec. 8, 2020).

> comparable information on a less frequent basis (*e.g.*, quarterly). Given that the Commission has proposed to grant substituted compliance with capital requirements, the frequency of financial reports required by an SBS Entity's home country regulator should also be sufficient for the Commission's purposes. Additionally, the Commission should set the submission deadline for Part II so that it aligns with the deadline for comparable reports to the SBS Entity's home country regulator.

Our members also continue to perform the line-by-line comparison between Part II and Part IIC, on the one hand, and the reports already submitted to the Commission, FRB, and home country supervisors, on the other hand, and we welcome continued discussions with Commission staff once this analysis is complete. In this regard, we continue to support the Commission's suggested approach of requiring SBS Entities covered by the Orders to satisfy their Rule 18a-7 obligations by completing a limited number of the required line items for two years. This approach would enable the Commission to evaluate further whether the scope of information that an SBS Entity provides to the Commission under the Orders in lieu of the full Part II or Part IIC, as applicable, might satisfactorily achieve the Commission's needs and if not, what changes need to be made. We welcome the opportunity to discuss with the Commission which aspects of Part II or Part IIC should be in-scope for this more limited reporting.

IX. MoU Regarding ECB-Owned Information

For certain SBS Entities, the AMF, ACPR, and ECB share responsibility for supervising compliance with some of the provisions of EU and French law addressed by the Proposal. There may be certain information related to such SBS Entities that is in the possession of the ECB or otherwise cannot be shared by the AMF and ACPR without the consent of the ECB. In the Proposal, the Commission noted that, to ensure it can obtain such ECB information, "the Commission and the ECB, and/or AMF and/or the ACPR . . . must have a memorandum of understanding and/or other arrangement addressing cooperation with respect to the Order as it pertains to this ECB-owned information."[38]

The Commission dealt with a similar issue in the German Order as the BaFin and the ECB share responsibility with respect to certain provisions of EU and German law. For purposes of the German Order, this condition was satisfied in the MoU between BaFin and the Commission. BaFin agreed, upon the request of the Commission, "to use its best efforts to assist the SEC in obtaining ECB information from the ECB in a prompt manner."[39] We request that the Commission confirm that if it receives similar assurances from the ACPR in an MoU or other arrangement, then such assurances will be sufficient for purposes of the final French Order, similar to the German Order.

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[38] Proposal at 85723.

[39] Memorandum of Understanding Concerning Consultation, Cooperation and the Exchange of Information Related to the Supervision and Oversight of Certain Cross-Border [OTC] Derivatives Entities In Connection with the Use of Substituted Compliance by Such Entities between the Commission and BaFin (Dec. 18, 2020).

* * *

SIFMA appreciates the opportunity to comment on the Proposal and the Commission's consideration of our views. SIFMA looks forward to continuing dialogue with the Commission regarding substituted compliance. If you have questions or would like additional information, please contact Kyle Brandon, at [redacted].

Very truly yours,

Kyle L Brandon
Managing Director, Head of Derivatives Policy
SIFMA

cc:

Honorable Allison Herren Lee, Acting Chairman, Securities and Exchange Commission
Honorable Hester M. Peirce, Commissioner, Securities and Exchange Commission
Honorable Elad L. Roisman, Commissioner, Securities and Exchange Commission
Honorable Caroline A. Crenshaw, Commissioner, Securities and Exchange Commission

Ms. Carol M. McGee, Assistant Director, Office of Derivatives Policy, Division of Trading and Markets, Securities and Exchange Commission
Ms. Laura Compton, Senior Special Counsel, Office of Derivatives Policy, Division of Trading and Markets, Securities and Exchange Commission

Enclosure

Annex: Summary of Prudential and Related Requirements Introduced or Amended by the French Implementation Texts of CRD V and CRR II

I. French Implementation of Prudential and Related Requirements of CRD V

CRD V has been implemented in France by:

- Ordinance no. 2020-1635 of 21 December 2020 on various provisions to adapt the legislation to EU law in financial matters;
- Decree no. 2020-1637 of 22 December 2020 on various provisions to adapt the legislation to EU law in financial matters and relating to finance companies;
- *Arrêté* of 22 December 2020 amending the *Arrêté* of 3 November 2014 relating to the capital buffers of banking service providers and investment firms other than portfolio management companies ("***Arrêté* of 22 December 2020 on capital buffers**"); and
- *Arrêté* of 22 December 2020 amending the *Arrêté* of 3 November 2014 relating to the internal control of companies in the banking, payment services and investment services sector subject to the supervision of the *Autorité de Contrôle Prudentiel et de Résolution*.

The provisions of such texts are generally applicable since December 29, 2020.

The changes to the prudential and related requirements brought by the implementation texts that entered into force are the following:

- ***Capital buffers***. The regime applicable to capital buffers is refined, and the procedure for the determination of their rate is simplified. The other systemically important institution ("**O-SII**") buffer rate can be raised up to 3% of the total risk exposure amount of credit institutions and investment firms (together hereinafter referred to as "**Institutions**") (previously, 2%), and above 3% with the approval of the European Commission. The definition and computation method of the systemic risk buffer is clarified. It may apply to all Institutions or a subset of Institutions, and may cover exposures located in certain countries or specific sectoral exposures. The maximum systemic buffer rate applicable to any of the covered exposures is set at 5%, but a higher rate may be set with the approval of the European Commission. Similarly, the approval of the European Commission is required where the sum of the O-SII buffer rate and of the systemic risk buffer rate is above 5%.[40]
- ***'Pillar 2' capital***. A distinction is introduced between the Pillar 2 requirements ("**P2R**") and the Pillar 2 guidance ("**P2G**"). P2R may be, under certain

[40] *Arrêté* of 22 December 2020 on capital buffers.

conditions, imposed by the competent supervisor in addition to "Pillar 1" capital requirements and capital buffers to cover elements of risks which are not fully captured by the minimum requirements. In addition, the competent supervisor may establish an additional own funds guidance. While P2G, unlike P2R, is not a legal minimum, Institutions are expected to follow guidance in order to be able to absorb potential losses resulting from crisis scenarios (*e.g.*, as identified in the context of supervisory stress tests). The competent supervisor is entitled to impose additional capital requirements to an Institution that repeatedly fails to meet its P2G.[41]

- ***Consequences in case of breach of prudential requirements***. The amendments clarify that the competent supervisor may withdraw the authorization of an Institution that (i) does not meet its Pillar 1 capital requirements, large exposures or liquidity requirements, (ii) does not comply with its P2R, (iii) can no longer be relied on to fulfil its obligations towards its creditors, and in particular, no longer ensures the safety of the assets entrusted to it by its depositors.[42] If a breach by an Institution of the prudential provisions may result in sanction proceedings being initiated against it, such proceedings may not be grounded on a breach of the minimum requirement for own funds and eligible liabilities ("**MREL**"), P2G, or on a breach of capital or leverage ratio buffers.[43] In case of a breach of the leverage ratio buffer, automatic restrictions on an Institution's ability to make certain distributions will be triggered and the Institution must submit a capital conservation plan to the relevant supervisor (as was already the case in the event of a breach of capital buffers).[44]

- ***Other***. The other amendments relate to (i) additional conditions for the authorization of credit institutions, (ii) consolidated supervision of a group, (iii) interest rate risk arising from non-trading book activities, (iv) governance, (v) remuneration policies, (vi) the conditions under which an intermediate EU parent undertaking must be established by a third-country group, (vii) the applicable regime and approval procedure for financial holding companies and mixed financial holding companies, and (viii) a refinement of certain provisions applicable to the competent supervisor and to cooperation and exchange of information between supervisory authorities or between the competent supervisor and international bodies.

II. CRR II Prudential and Related Requirements

CRR II has entered into force and is directly applicable in all EU Member States, including France. Part of its provisions are already applicable since June 27, 2019, including

[41] Monetary and Financial Code, Article L. 511-41-3.

[42] Monetary and Financial Code, Art. L. 511-15 and L. 532-6.

[43] Monetary and Financial Code, Art. L. 612-40.

[44] Monetary and Financial Code, Art. L. 511-41-1-A; *Arrêté* of 22 December 2020 on capital buffers.

provisions regarding total loss-absorbing capacity ("**TLAC**"), and the refinement of conditions under which instruments may qualify as common equity tier 1 ("**CET1**"), additional tier 1, or tier 2. Most of its provisions however will only become applicable on June 28, 2021, and the provisions regarding the leverage ratio buffer will apply from January 1, 2023.

The main changes to the prudential and related requirements are the following:

- ***Counterparty credit risk***. The exposure value of derivative transactions under the counterparty credit risk framework (the new standardised approach set by the Basel Committee and called "Standardised Approach for Counterparty Credit Risk") will apply to Institutions.

- ***Own funds requirements for market risk standards***. All Institutions subject to the fundamental review of the trading book framework (the revised standard developed by the BCBS) will need to start reporting the calculations derived from the revised standardized approach in order to allow for the finalisation of such framework on the basis of a delegated act adopted by the European Commission and amending the CRR. Publication of such delegated act is currently pending.

- ***Leverage ratio***. Institutions will be subject to a minimum leverage ratio requirement of 3%.

- ***Large exposures***. The regulatory capital that can be taken into account to calculate Institutions' large exposures limit will be limited to Tier 1 capital.

- ***Net stable funding ratio***. CRR II introduces a binding NSFR set at a minimum level of 100%, which requires Institutions to hold sufficient stable funding to meet their funding needs during a one-year period under both normal and stressed conditions. The NSFR has generally been implemented in accordance with the recommendations of the BCBS, with certain limited adjustments to take account of the European context. The requirement under the Basel NSFR to hold between 5% to 20% of stable funding against gross derivative liabilities has been introduced at a level of 5%, and may be amended in the future to take into account further developments at the Basel level.