

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-84991; File No. S7-27-11)

January 25, 2019

Order Granting a Limited Exemption from the Exchange Act Definition of “Penny Stock” for Security-Based Swap Transactions between Eligible Contract Participants; Granting a Limited Exemption from the Exchange Act Definition of “Municipal Securities” for Security-Based Swaps; and Extending Certain Temporary Exemptions under the Exchange Act in Connection with the Revision of the Definition of “Security” to Encompass Security-Based Swaps

I. Introduction

The Securities and Exchange Commission (“Commission” or “SEC”) is granting a limited exemption under Securities Exchange Act of 1934 (“Exchange Act”) from the definition of “penny stock” in Section 3a(51) and Rule 3a51-1 for transactions in security-based swaps between eligible contract participants (“ECPs”);¹ granting a limited exemption from the definition of “municipal securities” for security-based swaps; and extending until February 5, 2020, certain temporary exemptive relief originally provided by the Commission in connection with the revision of the definition of “security” in the Exchange Act to encompass security-based swaps.²

¹ The term “eligible contract participant” or “ECP” is defined in Section 1a(18) of the Commodity Exchange Act (“CEA”)[7 U.S.C. § 1a(18)]. The definition of the term “eligible contract participant” in the Exchange Act refers to the definition of “eligible contract participant” in the CEA. See Section 3(a)(65) of the Exchange Act. The SEC and the Commodity Futures Trading Commission have adopted final rules further defining the term “eligible contract participant.” See Further Definition of “Swap Dealer,” “Security-Based Swap Dealer,” “Major Swap Participant,” “Major Security-Based Swap Participant” and “Eligible Contract Participant,” Exchange Act Release No. 66868 (Apr. 27, 2012), 77 FR 30596 (May 23, 2012).

² See Order Granting Temporary Exemptions under the Securities Exchange Act of 1934 in Connection with the Pending Revisions of the Definition of “Security” to Encompass Security-Based Swaps, Exchange Act Release No. 64795 (July 1, 2011), 76 FR 39927 (July 7, 2011) (“2011 Exchange Act Exemptive Order”); See also Further Definition of “Swap,” “Security-Based Swap,” and “Security-Based Swap Agreement”; Mixed Swaps; Security-Based Swap Agreement Recordkeeping, Exchange Act Release No. 67453 (July 18, 2012), 77 FR 48207 (Aug. 13, 2012) (“Product Definitions Adopting Release”) (extending the expiration date of the Temporary Exemptions to February 11, 2013); Order Extending Temporary Exemptions under the Securities Exchange Act of 1934 in Connection with the Revision of the Definition of “Security” to Encompass Security-Based Swaps, and Request for Comment, Exchange Act Release No. 68864 (Feb. 7, 2013), 78 FR 10218 (Feb. 13, 2013) (extending the expiration date to February 11, 2014); Order Extending Temporary Exemptions under the Securities Exchange Act of 1934 in Connection with the Revision of the Definition of “Security” to

II. Discussion

A. Background

Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act³ amended the definition of “security” under the Exchange Act to expressly encompass security-based swaps.⁴ The expansion of the definition of the term “security” to include security-based swaps had the effect of changing the scope of the Exchange Act regulatory provisions that apply to security-based swaps and, in doing so, raised certain complex questions that required further consideration.

In July 2011, the Commission issued an order (the “2011 Exchange Act Exemptive Order”), which granted temporary exemptive relief from compliance with certain provisions of the Exchange Act in connection with security-based swap activity by: (i) any person who meets the definition of “eligible contract participant” set forth in Section 1a(12) of the Commodity Exchange Act as of July 20, 2010 (i.e., the day prior to the date the Dodd-Frank Act was signed into law) and (ii) a broker or dealer registered under Section 15(b) of the Exchange Act.⁵

Encompass Security-Based Swaps, and Request for Comment, Exchange Act Release No. 71485 (Feb. 5, 2014), 79 FR 7731 (Feb. 10, 2014) (“2014 Extension Order”) (extending the expiration date for certain Temporary Exemptions to February 5, 2017).; Order Extending Until February 5, 2019 Certain Temporary Exemptions under the Securities Exchange Act of 1934 in Connection with the Pending Revision of the Definition of “Security” to Encompass Security-Based Swaps and Request for Comment, Exchange Act Release No. 82626 (Feb. 2, 2018), 83 FR 5665 (Feb. 18, 2018) (“2018 Extension Order”).

³ The Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010) (“Dodd-Frank Act”).

⁴ See Section 761(a)(2) of the Dodd-Frank Act (amending Section 3(a)(10) of the Exchange Act (15 U.S.C. 78c(a)(10)). The provisions of Title VII generally became effective on July 16, 2011 (360 days after the enactment of the Dodd-Frank Act) (the “Effective Date”), unless a provision required a rulemaking, in which case the provision would go into effect “not less than” 60 days after publication of the related final rules in the Federal Register or on July 16, 2011, whichever is later. See Section 774 of the Dodd-Frank Act (15 U.S.C. 77b).

The overall approach of the 2011 Exchange Act Exemptive Order was directed toward maintaining the status quo during the implementation process for the Dodd-Frank Act.⁶ In the 2011 Exchange Act Exemptive Order, the Commission stated that it would accomplish this “by preserving the application of particular Exchange Act requirements that already are applicable in connection with instruments that will be ‘security-based swaps’ following the Effective Date [of the Dodd-Frank Act], but deferring the applicability of additional Exchange Act requirements in connection with those instruments explicitly being defined as ‘securities’ as of the Effective Date.”⁷

In 2014, the Commission extended the expiration dates for the temporary exemptions in the 2011 Exchange Act Exemptive Order.⁸ In the 2014 Extension Order, the Commission distinguished between: (i) the temporary exemptions related to pending security-based swap rulemakings (“Linked Temporary Exemptions”); and (ii) the temporary exemptions that generally were not directly related to a specific security-based swap rulemaking (“Unlinked Temporary Exemptions”).⁹ The expiration dates for the Linked Temporary Exemptions established by the 2014 Extension Order were the compliance dates for the specific rulemakings

⁵ See 2011 Exchange Act Exemptive Order, 76 FR at 39938–39. The 2011 Exchange Act Exemptive Order did not provide exemptive relief for any provisions or rules prohibiting fraud, manipulation, or insider trading (other than the prophylactic reporting or recordkeeping requirements such as the confirmation requirements of Exchange Act Rule 10b-10). In addition, the 2011 Exchange Act Exemptive Order did not affect the Commission’s investigative, enforcement, and procedural authority related to those provisions and rules. See 2011 Exchange Act Exemptive Order at 39931, n. 34. The 2011 Exchange Act Exemptive Order also did not address Sections 12, 13, 14, 15(d), 16, and 17A of the Exchange Act and the rules thereunder.

⁶ See id., at 39929.

⁷ Id. Under the 2011 Exchange Act Exemptive Order, instruments that (before the Effective Date) were security-based swap agreements and (after the Effective Date) constituted security-based swaps were still subject to the application of those Exchange Act provisions. See 2011 Exchange Act Exemptive Order, 76 FR at 39930, nn. 24–25.

⁸ See 2014 Extension Order.

⁹ See id., at 7732.

to which they were “linked,” and the expiration date for the Unlinked Temporary Exemptions was three years following the effective date of the 2014 Extension Order (i.e., February 5, 2017), or such time that the Commission issues an order or rule determining whether continuing exemptive relief is appropriate for security-based swaps with respect to any such Unlinked Temporary Exemptions. This approach was designed to provide the Commission with flexibility while its Dodd-Frank Act rulemaking is still in progress to determine whether continuing relief should be provided for any of the Unlinked Temporary Exemptions.¹⁰

2018 Extension Order

In the 2018 Extension Order, the Commission extended the expiration date of the Unlinked Temporary Exemptions until February 5, 2019.¹¹ In the 2018 Extension Order, the

¹⁰ See id., at 7731. The 2014 Extension Order referred to the temporary exemptions provided for in the 2011 Exchange Act Exemptive Order as the “Expiring Temporary Exemptions” and noted that the 2011 Exchange Act Exemptive Order generally provided for the following exemptions from the Exchange Act: “(a) temporary exemptions in connection with security-based swap activity by certain ‘eligible contract participants’; and (b) temporary exemptions specific to security-based swap activities by registered brokers and dealers.”

The 2014 Extension Order identified the Linked Temporary Exemptions as those Expiring Temporary Exemptions related to: (1) capital and margin requirements applicable to a broker or dealer (Sections 7 and 15(c)(3), Regulation T, and Exchange Act Rules 15c3-1, 15c3-3, and 15c3-4); (2) recordkeeping requirements applicable to a broker or dealer (Sections 17(a) and 17(b) and Exchange Act Rules 17a-3, 17a-4, 17a-5, 17a-11, and 17a-13); (3) registration requirements under Section 15(a)(1), and the other requirements of the Exchange Act and the rules and regulations thereunder that apply to a “broker” or “dealer” that is not registered with the Commission; (4) Exchange Act Rule 10b-10; and (5) Regulation ATS. The remaining Expiring Temporary Exemptions are the Unlinked Temporary Exemptions.

As applicable, the Commission extended the Linked Temporary Exemptions until the compliance date for pending rulemakings concerning: capital, margin, and segregation requirements for security-based swap dealers and major security-based swap participants; recordkeeping and reporting requirements for broker-dealers, security-based swap dealers, and major security-based swap participants; security-based swap trade acknowledgements; and registration requirements for security-based swap execution facilities. The Linked Temporary Exemptions are not addressed in this order and have been, or will be, separately considered in connection with the related security-based swap rulemakings. See, e.g., Trade Acknowledgement and Verification of Security-Based Swap Transactions, Exchange Act Release No. 78011 (June 8, 2016), 81 FR 39807, 39824-25, n. 189 (June 17, 2016).

¹¹ See 2018 Extension Order. See also Order Extending Certain Temporary Exemptions under the Securities Exchange Act of 1934 in Connection with the Revision of the Definition of “Security” to Encompass Security-Based Swaps and Request for Comment, Exchange Act Release No. 79833 (Jan. 18, 2017), 82 FR 8467 (Jan. 25, 2017) (“2017 Extension Order”). The 2017 Extension Order, which had extended the expiration date of the

Commission also requested comment on whether continuing exemptive relief is necessary beyond February 5, 2019.¹² The Commission received four letters from two different commenters in response.¹³

B. Temporary Exemptions

The Commission has proposed substantially all of the rules governing security-based swap market participants and transactions required by Title VII of the Dodd-Frank Act and has finalized a majority of these rulemakings.¹⁴ However, the Commission is still in the process of finalizing some remaining rules under Title VII of the Dodd-Frank Act.¹⁵

Unlinked Temporary Exemptions until February 5, 2018, received two comments, both of which had expressed support for extending the exemptive relief, with one reiterating its prior request that the Commission provide permanent exemptive and other relief to security-based swap market participants from the Exchange Act and the Securities Act. See comment from Layla Spencer, dated Jan. 30, 2017; and letters from Kyle Brandon, Managing Director, SIFMA, dated Feb. 2, 2017 (“SIFMA Letter I”) and Jan. 11, 2018 (“SIFMA Letter II”) (requesting that the Commission further extend the exemptive relief for the Unlinked Temporary Exemptions). For details regarding SIFMA’s earlier request for permanent exemptive and other relief, see Draft SIFMA SBS Exemptive Relief Request (Oct. 20, 2011), which is available at <https://www.sec.gov/comments/s7-27-11/s72711-7.pdf>, and SIFMA SBS Exemptive Relief Request (Dec. 5, 2011), which is available at <https://www.sec.gov/comments/s7-27-11/s72711-10.pdf>.

¹² Comments received are available at <https://www.sec.gov/comments/s7-27-11/s72711.shtml>. The Commission did not receive any comments in response to the request for comment in the 2014 Extension Order. However, in 2012, the Commission received a request from market participants to extend certain of the Temporary Exemptions, citing concerns that key issues and questions regarding the application of the federal securities laws remained unresolved and continuing concerns about the potential for unnecessary disruption to the security-based swap market. See SIFMA Request for Extension of the Expiration Date of the SEC’s Exchange Act Exemptive Order and SBS Interim final Rules (Dec. 20, 2012), which is available at <http://www.sec.gov/comments/s7-27-11/s72711-12.pdf>.

¹³ See letter from Kyle Brandon, Managing Director, SIFMA, dated Nov. 8, 2018 (“SIFMA Letter III”) (requesting that the Commission further extend the exemptive relief for the Unlinked Temporary Exemptions, which are currently set to expire on Feb. 5, 2019, and also requesting certain permanent exemptive and other relief). See also supplemental letter from Kyle Brandon, Managing Director, SIFMA, dated Dec. 20, 2018 (“SIFMA Letter IV”) (supplementing November 2018 submission with additional detail and recommending a transition period before expiration of any Unlinked Temporary Exemptions). See also letters from Walt L. Lukken, President and Chief Executive Officer, Futures Industry Association, dated Nov. 18 and Nov. 29, 2018 (the “FIA Letters”) (each expressing support for codifying the exemptions for SBS from inapplicable securities rules).

¹⁴ See, e.g., Regulation SBSR—Reporting and Dissemination of Security-Based Swap Information, Exchange Act Release No. 74244 (Feb. 11, 2015), 80 FR 14563 (Mar. 19, 2015); Security-Based Swap Data Repository Registration, Duties, and Core Principles, Exchange Act Release No. 74246 (Feb. 11, 2015), 80 FR 14437 (Mar. 19, 2015); Registration Process for Security-Based Swap Dealers and Major Security-Based Swap Participants,

As described above, since initially granting temporary exemptive relief for the Unlinked Temporary Exemptions, the Commission has extended the temporary exemptive relief four times. Each time, the Commission requested comment on why continuing the exemptive relief was necessary. In 2018, the Commission requested that “any request should be detailed as to the circumstances in which the Exchange Act provision or rule applies to security-based swaps or security-based swap market participants, and why relief [would be] necessary.”¹⁶ Detailed comments could provide the Commission with information useful to evaluate whether an exemption is necessary or appropriate in the public interest, and consistent with the protection of investors, as required by Section 36.¹⁷

Following its issuance of the 2018 Extension Order, the Commission received four letters from two different commenters that were responsive to the request for comment in the 2018 Extension Order. Two of the letters from one commenter identified specific provisions for

Exchange Act Release No. 75611 (Aug. 5, 2015), 80 FR 48963 (Aug. 14, 2015); Regulation SBSR—Reporting and Dissemination of Security-Based Swap Information, Exchange Act Release No. 78321 (July 14, 2016), 81 FR 53545 (Aug. 12, 2016); Applications by Security-Based Swap Dealers or Major Security-Based Swap Participants for Statutorily Disqualified Associated Person To Effect or Be Involved in Effecting Security-Based Swaps, Exchange Act Release No. 84858 (Dec. 19, 2018).

¹⁵ See, e.g., Registration and Regulation of Security-Based Swap Execution Facilities, Exchange Act Release No. 63825 (Feb. 2, 2011), 76 FR 10948 (Feb. 28, 2011); Capital, Margin, and Segregation Requirements for Security-Based Swap Dealers and Major Security-Based Swap Participants and Capital Requirements for Broker-Dealers, Exchange Act Release No. 68071 (Oct. 18, 2012), 77 FR 70213 (Nov. 23, 2012); Recordkeeping and Reporting Requirements for Security-Based Swap Dealers, Major Security-Based Swap Participants, and Broker-Dealers; Capital Rule for Certain Security-Based Swap Dealers; Proposed Rules, Exchange Act Release No. 71958 (Apr. 17, 2014), 79 FR 25194 (May 2, 2014); Risk Mitigation Techniques for Uncleared Security-Based Swaps, Exchange Act Release No. 84861 (Dec. 19, 2018).

¹⁶ See 2018 Extension Order, at 8469.

¹⁷ See Exchange Act Section 36 [15 U.S.C. §78mm]. Section 36 of the Exchange Act authorizes the Commission to conditionally or unconditionally exempt, by rule, regulation, or order any person, security, or transaction (or any class or classes of persons, securities, or transactions) from any provision of the Exchange Act or any rule or regulation.

which permanent relief was sought.¹⁸ In particular, in SIFMA Letter III and SIFMA Letter IV, SIFMA requests (1) that two of the exemptions it describes as implicated by the Unlinked Temporary Exemptions (exemptions from the definition of “penny stock” and from Section 31 fees for security-based swaps) be extended on a permanent basis; and (2) guidance regarding municipal and government securities. In SIFMA Letter III, SIFMA also requests that the Commission provide an additional extension period before the expiration of the remaining Unlinked Temporary Exemptions in order to allow for an orderly transition. In SIFMA Letter IV, SIFMA clarifies that request for an additional extension period and requests that the Commission extend the Unlinked Temporary Exemptions for an additional twelve months. The FIA Letters express support for SIFMA Letter III and for extending the temporary exemptive relief for the Unlinked Temporary Exemptions beyond February 5, 2019.¹⁹

In SIFMA Letter III and SIFMA Letter IV, SIFMA requests additional relief not discussed in this Order.²⁰ In particular, SIFMA requests relief in relation to the (i) regulation of security-based swap execution facilities, (ii) broker-dealer registration, (iii) Exchange Act Rule 10b-10, (iv) margin, (v) hypothecation, (vi) disclosure requirements relating to extensions of credit, (vii) requirements relating to personnel of SBS Entities, (viii) research requirements, (ix) municipal advisor regulation, (x) securities activities of OTC Derivatives Dealers, (xi) Exchange Member SRO Membership, and (xii) Audit Committees and Compensation Committees.²¹ Some of these requests relate to Linked Temporary Exemptions rather than Unlinked Temporary

¹⁸ See SIFMA Letters III and IV, supra note 13.

¹⁹ See FIA Letters, supra note 13.

²⁰ See SIFMA Letter III and SIFMA Letter IV, supra note 13.

²¹ See SIFMA Letter III, supra note 13.

Exemptions, and, as noted above, the Commission has considered or will consider those requests in connection with the related security-based swap rulemakings. In addition, the Commission believes that all of the additional requests would benefit from further consideration. The Commission invites market participants or other interested parties to provide any information that may be relevant to the Commission’s consideration of these requests for relief, or to the scope of the order more generally.

C. Penny Stocks

In SIFMA Letter III, SIFMA requests an exemption from the definition of “penny stock” in Exchange Act Section 3(a)(51) and Exchange Act Rule 3a51-1 for security-based swap transactions between ECPs. SIFMA notes that it may not always be clear that a security-based swap is not a “penny stock” because the price of the security-based swap in dollar terms may not always be clear, and requests that the Commission provide certainty with respect to transactions between ECPs.²² In SIFMA Letter IV, SIFMA also adds that it is not clear which security-based swaps constitute equity securities or whether, in classifying security-based swaps as penny stocks, market participants should evaluate the security-based swap itself or its underlier.²³ SIFMA also argues that the requirements applicable to penny stocks under Rules 15g-1 through 15g-9 are designed to apply to cash market securities transactions, not over-the-counter security-based swaps.²⁴ Moreover, according to SIFMA, security-based swaps will be subject to enhanced security-based swap specific disclosure and sales practice requirements as part of the

²² See SIFMA Letter III, supra note 13.

²³ See SIFMA Letter IV, supra note 13.

²⁴ Id.

Commission's business conduct standards for security-based dealers and major security-based swap participants, making the penny stock regulation duplicative.²⁵

The definition of "penny stock" and the associated rules were part of a comprehensive effort by Congress and the Commission to reduce fraud and manipulation in the penny stock market and to address, among other things, a lack of investor information and education.²⁶ In the Securities Enforcement Remedies and Penny Stock Reform Act of 1990, Congress directed the Commission to adopt a series of rules requiring broker-dealers to provide customers with certain trade and market information prior to effecting a transaction in a penny stock for their customers.²⁷ Rules 15g-1 through 15g-9 under the Exchange Act (collectively known as the "penny stock rules") implement the Congressional directive to increase the level of disclosure to investors concerning penny stocks generally as well as the specific penny stock involved in a transaction.²⁸ The scope of the penny stock rules is delineated by the definition of penny stock in Exchange Act Section 3(a)(51)²⁹ and Rule 3a51-1³⁰ thereunder.

The Dodd-Frank Act established a comprehensive framework for regulating the over-the-counter security-based swap market.³¹ As part of that framework, Dodd-Frank directed the Commission to establish business conduct standards for security-based swap dealers and major-

²⁵ Id.

²⁶ Pub. L. No. 101-429, 104 Stat. 931 (1990); See Penny Stock Disclosure Rules, Exchange Act Release No. 30608 (Apr. 20, 1992), 57 FR 18004 (Apr. 28, 1992).

²⁷ Id.

²⁸ Exchange Act Section 15(h) [15 U.S.C. §78o(h)].

²⁹ Exchange Act Section 3(a)(51) [15 U.S.C. §78c(a)(51)].

³⁰ Exchange Act Rule 3a51-1 [17 CFR 240.3a51-1].

³¹ Dodd-Frank Act.

security-based swap participants.³² In light of that framework, the Commission agrees with SIFMA’s statement that transactions in security-based swaps will be subject to security-based swap specific disclosures and sales practices.³³ Although those Dodd-Frank disclosures and sales practices may not be precisely the same as those required under the penny stock rules, the Commission believes that the additional protections of the penny stock rules are unnecessary for transactions in security-based swaps with ECPs,³⁴ who, with respect to security-based swaps, are generally the type of market participants who understand the risks of security-based swaps without needing the added protections provided for by the penny stock rules.³⁵

Accordingly, the Commission finds it is appropriate and in the public interest and consistent with the protection of investors to provide a new exemption from the definition of “penny stock” in Section 3(a)(51) and Rule 3a51-1 for security-based swap transactions between ECPs.

D. Municipal Securities

In its letters, SIFMA asked for guidance that, for purposes of the Exchange Act, including Section 15B and rules thereunder applicable to municipal securities, a security-based swap with a counterparty that is a municipal entity should not be considered a municipal security

³² See Dodd-Frank Act Section 764(h). Business Conduct Standards for Security-Based Swap Dealers and Major Security-Based Swap Participants, Release 34-77617 (Apr. 14, 2016), 81 FR 29960 (May 13, 2016) (“Business Conduct Standards Adopting Release”). This includes standards for when those entities act as advisors to “special entities” or engaging in security-based swap transactions with counterparties, including those that are special entities.

³³ See Exchange Act Rules 15Fh-1 through 15Fh-6 and Rule 15Fk-1.

³⁴ Many transactions in security-based swaps with ECPs will already be exempt from the penny stock rules, given the exemption provided for transactions that meet the requirements of Regulation D or transactions with an issuer not in connection with a public offering pursuant to Section 4(a)(2) of the Securities Act of 1933. See Exchange Act Rule 15g-1(c).

³⁵ The 2011 Exchange Act Exemptive Order did not provide relief for transactions with non-ECPs.

solely due to the identity of the counterparty. Exchange Act Section 3(a)(29) defines the term “municipal securities” to include “securities which are direct obligations of, or obligations guaranteed as to principal or interest by, a State or any political subdivision thereof, or any agency or instrumentality of a State or any political subdivision thereof, or any municipal corporate instrumentality of one or more States.”³⁶ The Commission understands that there is some uncertainty among market participants regarding whether Exchange Act regulatory provisions that apply to municipal securities brokers³⁷ and municipal securities dealers³⁸ apply to security-based swap dealers and major security-based swap participants that enter into security-based swaps with a counterparty that is a State or any political subdivision thereof, or any agency or instrumentality of a State or any political subdivision thereof, or any municipal corporate instrumentality of one or more States (a “municipal counterparty”). As noted above with respect to the penny stock rules, security-based swap dealers and major security-based swap participants are already subject to a comprehensive regulatory regime. Moreover, that regulatory regime includes specific protections for when a security-based swap dealer or major security-based swap participant is acting as counterparty to a “special entity,” including a State, State agency, city,

³⁶ See Exchange Act Section 3(a)(29) [15 U.S.C. §78c(a)(29)].

³⁷ Section 3(a)(31) of the Exchange Act defines the term “municipal securities broker” to mean “a broker engaged in the business of effecting transactions in municipal securities for the account of others.” See Exchange Act Section 3(a)(31) [15 U.S.C. §78c(a)(31)].

³⁸ Exchange Act Section 3(a)(30) defines the term “municipal securities dealer” to mean “any person (including a separately identifiable department or division of a bank) engaged in the business of buying and selling municipal securities for his own account, through a broker or otherwise, but does not include—(A) any person insofar as he buys or sells such securities for his own account, either individually or in some fiduciary capacity, but not as a part of a regular business; or (B) a bank, unless the bank is engaged in the business of buying and selling municipal securities for its own account other than in a fiduciary capacity, through a broker or otherwise; Provided, however, that if the bank is engaged in such business through a separately identifiable department or division (as defined by the Municipal Securities Rulemaking Board in accordance with section 15B(b)(2)(H) of the Exchange Act), the department or division and not the bank itself shall be deemed to be the municipal securities dealer.” See Exchange Act Section 3(a)(30) [15 U.S.C. §78c(a)(30)].

county, municipality, or other political subdivision of a State.³⁹ Given the comprehensive scope of this regulatory regime and for the avoidance of doubt, the Commission finds that it is appropriate and in the public interest to provide an exemption from the definition of “municipal securities” in Section 3(a)(29) for security-based swap transactions with a municipal counterparty. In the Commission’s view, the exemption will avoid the application of duplicative and potentially conflicting requirements to security-based swap dealers and major security-based swap participants.

E. Government Securities

In SIFMA Letter III and SIFMA Letter IV, SIFMA asked for guidance that, for purposes of the Exchange Act, including Section 15C and rules thereunder applicable to government securities, a security-based swap with a counterparty that is a “U.S. government-related entity” should not be considered a government security solely due to the identity of the counterparty. The Unlinked Temporary Exemptions did not provide such relief and, thus, the treatment of government securities will not be impacted by the expiration of the Unlinked Temporary Exemptions. For that reason, the Commission is not addressing the subject of government securities as part of this Order. The Commission may consider SIFMA’s request with respect to government securities, as well as the other requests included in SIFMA Letter III and SIFMA Letter IV, at a later date.⁴⁰

³⁹ See Exchange Act Section 15(h)(4)-(5). [15 U.S.C. §78o-10(h)(4)-(5)].

⁴⁰ Exchange Act Section 36(b) provides that “the Commission may not, under this section, exempt any person, security, or transaction, or any class or classes of persons, securities, or transactions from Section 15C or the rules or regulations issued thereunder or (for purposes of section 15C and the rules and regulations issued thereunder) from any definition in paragraph (42), (43), (44), or (45) of section 3(a).” [15 U.S.C. §78mm].

F. Section 31 Fees

In SIFMA Letter III, SIFMA requested guidance that security-based swap transactions are not subject to Section 31 fees merely because they are subject to transaction reporting under Regulation SBSR. The Commission is not providing relief from Section 31 at this time. A sale of a security is subject to Section 31 fees only if (1) the sale occurs on a national securities exchange,⁴¹ or (2) the sale is transacted by or through a member of a national securities association otherwise than on a national securities exchange and the security is registered on a national securities exchange or subject to prompt last-sale reporting pursuant to the rules of the Commission or a registered national securities association.⁴² Although security-based swaps are securities, they do not meet any of the conditions noted above. Thus, security-based swaps are currently not subject to Section 31 fees and would not become subject to Section 31 fees due to the expiration of the Unlinked Temporary Exemptions or the full implementation of Regulation SBSR as it currently exists.

The Dodd-Frank Act created a new Section 13(m) of the Exchange Act that requires “real-time public reporting” of security-based swap transactions. Once real-time public reporting is fully-implemented, security-based swaps will be subject to prompt last-sale reporting pursuant to the rules of the Commission, which will subject them to Section 31 fees. Thus, when the Commission proposes to implement prompt last-sale reporting for security-based swap transactions, it may also revisit the appropriateness of exempting security-based swaps from Section 31 fees at such time.

⁴¹ See Exchange Act Section 31(b) [15 U.S.C. §78ee(b)].

⁴² See Exchange Act Section 31(c) [15 U.S.C. §78ee(c)].

G. Transition Period

In SIFMA Letter III, SIFMA requested that the Unlinked Temporary Exemptions for which permanent relief is not granted be extended until the date when security-based swap dealers and major-security-based swap participants are required to register with the Commission. In SIFMA Letter IV, SIFMA requested a twelve month transition period. SIFMA stated that the expiration of the Unlinked Temporary Exemptions will result in the application or potential application of over 150 different Exchange Act provisions.⁴³ SIFMA stated that market participants could design and implement appropriate compliance measures and controls during that transition period.⁴⁴ The Commission agrees that a transition period is appropriate. The Commission agrees that a twelve month transition period should allow market participants adequate time to design and implement appropriate compliance measure and controls. With this Order, the Commission is providing notice that the majority of the Unlinked Temporary Exemptions will expire on February 5, 2020, in order to provide sufficient additional time for market participants to prepare.

III. Commission Findings

The Commission believes it is necessary or appropriate in the public interest, and consistent with the protection of investors to extend for a period twelve months, the Unlinked Temporary Exemptions, until February 5, 2020, to allow market participants to prepare for the application of certain Exchange Act provisions and rules to security-based swap activities. The additional extension period will apply to all of the Unlinked Temporary Exemptions otherwise set to expire on February 5, 2019. Once this twelve-month extension period ends, all of the

⁴³ See SIFMA Letter IV, supra note 13.

⁴⁴ Id.

Unlinked Temporary Exemptions will expire, with the exception of the exemptions being provided with respect to the regulation of penny stocks involving only ECPs and with respect to the definition of municipal securities, as described above. As noted above, the Commission invites market participants or other interested parties to provide comments regarding the scope of the permanent relief the Commission is granting in this order, including whether the Commission should provide further relief in response to specific requests made by prior commenters that the Commission is not addressing at this time.

Accordingly, pursuant to its authority under Section 36 of the Exchange Act,⁴⁵ the Commission believes it is necessary or appropriate in the public interest, and consistent with the protection of investors to extend the expiration of all Unlinked Temporary Exemptions for a period of twelve months (i.e., until February 5, 2020).

Pursuant to Sections 36, the Commission finds that it is necessary and appropriate and in the public interest, and consistent with the protection of investors to provide an exemption or security-based swap transactions between ECPs from the definition of “penny stock” in Exchange Act Section 3a(51) and Exchange Act Rule 3a51-1.

Pursuant to Section 36, the Commission finds that it is necessary and appropriate and in the public interest, and consistent with the protection of investors to provide for an exemption for security-based swap transactions with a municipal counterparty from the definition of “municipal securities” in Exchange Act Section 3(a)(29).

* * * * *

⁴⁵ Exchange Act Section 36 [15 U.S.C. §78mm]. Section 36 of the Exchange Act authorizes the Commission to conditionally or unconditionally exempt, by rule, regulation, or order any person, security, or transaction (or any class or classes of persons, securities, or transactions) from any provision of the Exchange Act or any rule or regulation thereunder, to the extent such exemption is necessary or appropriate in the public interest, and is consistent with the protection of investors.

IV. Conclusion

IT IS HEREBY ORDERED, pursuant to Section 36 of the Exchange Act, that except as provided below, the Unlinked Temporary Exemptions contained in the 2011 Exchange Act Exemptive Order, and extended in the 2018 Extension Order, in connection with the revision of the Exchange Act definition of “security” to encompass security-based swaps, are extended until February 5, 2020.

IT IS FURTHER ORDERED, pursuant to Section 36 of the Exchange Act, that security-based swap transactions between ECPs shall be exempt from the definition of “penny stock” set forth in Exchange Act Section 3(a)(51) and Rule 3a51-1.

IT IS FURTHER ORDERED, pursuant to Section 36 of the Exchange Act, that security-based swaps shall be exempt from the definition of “municipal securities” in Exchange Act Section 3(a)(29).

By the Commission.

Eduardo A. Aleman
Deputy Secretary