SEC Issues FAQs on Federal Broker-Dealer Registration Exemption for Foreign Broker-Dealers

The staff of the U.S. Securities and Exchange Commission (“SEC”) recently published responses to certain frequently asked questions (“FAQs”) concerning the application of Rule 15a-6 under the Securities Exchange Act of 1934, as amended (“Exchange Act”), which provides conditional exemptions from the Exchange Act’s broker-dealer registration provisions for certain non-U.S. resident brokers and dealers.1

Overview of Rule 15a-6

The Exchange Act’s broker-dealer registration provisions generally provide that any “broker” or “dealer,” wherever organized or operated, that uses the U.S. mail or any means or instrumentality of U.S. interstate commerce to solicit or effect transactions in securities must register with the SEC, absent an available exemption.2

The SEC adopted Rule 15a-6 (“Rule”) in 19893 in order to provide four conditional exemptions from this registration requirement for certain non-U.S. resident brokers and dealers that limit their securities activities with, or on behalf of, U.S. persons to:

- transactions with and for U.S. persons who have not been solicited by the broker-dealer (Rule 15a-6(a)(1));
- dissemination of research reports to “major U.S. institutional investors” and the effecting of transactions in securities that are the subject of such reports, subject to certain conditions (Rule 15a-6(a)(2));
- solicitation of “U.S. institutional investors” and “major U.S. institutional investors,” provided that any subsequent transactions are effectuated through a U.S. registered broker-dealer and the U.S. broker-dealer follows detailed “chaperoning” requirements in connection with the non-U.S. broker-dealer’s activities in the United States (Rule 15a-6(a)(3)); and
- solicitation of certain exempted parties (including U.S. registered broker-dealers, U.S. or State-regulated banks acting pursuant to an exception or exemption from the Exchange Act’s “broker” or “dealer” definitions, and non-U.S. persons temporarily present in the United States) and effecting any resulting transactions with or for such exempted parties (Rule 15a-6(a)(4)).

2 Subject to certain exceptions, the Exchange Act defines a “broker” generally as any person engaged in the business of effecting transactions in securities for the account of others, and a “dealer” generally as any person engaged in the business of buying and selling securities for such person’s own account, whether through a broker or otherwise.
The Rule’s conditional exemptions are available only to a “foreign broker or dealer,” which the Rule defines generally as any non-U.S. resident person “that is not an office or branch of, or a natural person associated with, a registered broker or dealer, whose securities activities, if conducted in the United States, would be described by the [Exchange Act’s] definition of ‘broker’ or ‘dealer.’” Non-U.S. resident brokers and dealers meeting this definition are collectively referred to herein as “foreign broker-dealers.”

Prior guidance on the operation of Rule 15a-6 and the four categories of exempted activity has been provided through various SEC no-action letters and releases, as well as responses to frequently asked questions regarding the application of Regulation AC to the research activities of foreign broker-dealers.

The New Rule 15a-6 FAQs and Their Relationship to Historical Guidance

The SEC staff continues to receive numerous questions regarding the application of Rule 15a-6. The FAQs discuss some of the most frequently asked questions and the staff’s responses thereto. Following is a discussion of the FAQs and their relationship to the Rule’s provisions and historical SEC staff interpretations regarding the Rule’s operation.

Interpretation of “Major U.S. Institutional Investor” Definition as Used Throughout the Rule

Rule 15a-6 allows foreign broker-dealers to engage in certain activities with “major U.S. institutional investors.” The Rule defines a “major U.S. institutional investor” as (i) a “U.S. institutional investor” that has, or has under management, total assets in excess of $100 million; or (ii) a U.S. registered investment adviser that has total assets under management in excess of $100 million.

In 1997, the SEC staff’s Nine Firms Letter took the interpretive position that foreign broker-dealers affiliated with a U.S. registered broker-dealer may treat all U.S. institutions owning or controlling in excess of $100 million in aggregate “financial assets” as “major U.S. institutional investors” for purposes of the Rule. FAQ 6 clarifies that foreign broker-dealers that are not affiliated with a U.S. broker-dealer may also rely upon this expanded interpretation of the “major U.S. institutional investor” definition. FAQ 7 reaffirms that the expanded interpretation applies to all provisions of Rule 15a-6 in which the definition is used.

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6 A “U.S. institutional investor” is, in turn, defined in the Rule as (i) a U.S. registered investment company; (ii) a bank, savings and loan association, insurance company, business development company, or employee benefit plan defined in Rule 501(a)(1) of Regulation D; (iii) a private business development company defined in Rule 501(a)(2) of Regulation D; (iv) a Rule 501(c)(3) organization, as described in Rule 501(a)(3) of Regulation D; or (v) a trust defined in Rule 501(a)(7) of Regulation D.

7 See supra note 4.


Unsolicited Transactions (Rule 15a-6(a)(1))

Rule 15a-6(a)(1) permits a foreign broker-dealer to effect securities transactions with or for U.S. persons that have not been solicited by the broker or dealer. While Rule 15a-6 does not define the term “solicited,” the SEC has historically interpreted the term broadly (and thus the exemption narrowly) for purposes of Rule 15a-6 to include “any affirmative effort by a broker or dealer intended to induce transactional business for the broker-dealer or its affiliates,” including “efforts to induce a single transaction or to develop an ongoing securities business relationship.”

Multiple transactions with the same U.S. investor. FAQ 9 states that a foreign broker-dealer is not necessarily precluded from effecting multiple transactions on behalf of the same U.S. investor in reliance on Rule 15a-6(a)(1), absent other indicia of solicitation. At the same time, the FAQ notes that the SEC staff would likely view a significant number of transactions between a foreign broker-dealer and a U.S. investor as being indicative of solicitation through the establishment of an “ongoing securities business relationship.”

Delivery of certain transaction-related documents. FAQ 3 makes clear that providing an unsolicited U.S. investor with certain transaction-related documents required by applicable foreign law (e.g., a confirmation or account statement, or a prospectus, proxy statement or privacy notice) would not constitute solicitation without further action by the foreign broker-dealer. Foreign broker-dealers relying upon the unsolicited transactions exemption may not, however, provide U.S. investors with advertising materials or other documents intended to induce securities transactions.

Administration of non-U.S. issuers’ employee benefit plans. FAQ 2 states that a foreign broker-dealer administering a global employee stock option plan (“ESOP”) or other employee benefit plan for a foreign issuer that is organized outside the United States and whose principal office and place of business is located outside of the United States would not be considered to have solicited the foreign issuer’s U.S. employees or U.S. subsidiaries solely through such activity, provided certain conditions are met.

Provision of Research Reports to Major US Institutional Investors (Rule 15a-6(a)(2))

Pursuant to Rule 15a-6(a)(2), a foreign broker-dealer also is permitted to furnish research reports on securities directly to “major U.S. institutional investors” and to effect transactions in those securities with or for such institutional investors, provided certain conditions are satisfied. Among other things, (i) the research reports must not recommend the use of the foreign broker-dealer to effect trades in any security, (ii) if the foreign broker-dealer has a “chaperoning” relationship with a U.S. registered broker-dealer, transactions with the foreign broker or dealer in securities discussed in the research reports must be effected through that registered broker-dealer, pursuant to the chaperoning provisions of Rule 15a-6(a)(3), and (iii) the foreign broker-dealer may not provide research to U.S. persons pursuant to any express or implied understanding that those U.S. persons will direct commission income to the foreign broker-dealer.

Expanded interpretation of “major U.S. institutional investor” definition applies. As previously noted, FAQs 6 and 7 make clear that the Nine Firms Letter’s expanded interpretation of the “major US institutional investor”

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10 Adopting Release, supra note 3, at 54 FR 30017, 30018. Specific examples of conduct deemed to be solicitation for purposes of the Rule include: (i) telephone calls encouraging use of the foreign broker-dealer to effect securities transactions; (ii) advertising of the foreign broker-dealer’s services that is directed into the United States; (iii) conducting investment seminars for U.S. investors; or (iv) recommending the purchase or sale of securities, with the anticipation that the investor will execute the recommended trade through the foreign broker-dealer. Id.

11 The SEC has indicated that the exception in Rule 15a-6(a)(1) for unsolicited trades is designed to reflect the view that “U.S. persons seeking out unregistered foreign broker-dealers outside the United States cannot expect the protection of U.S. broker-dealer standards.” Adopting Release at 54 FR 30031. As the FAQs note, the SEC believes that a U.S. investor might reasonably expect to be protected by U.S. laws and regulations where a foreign broker-dealer regularly effects transactions with or for the investor. See also Exchange Act Release No. 25801 under “Solicitation of U.S. Investors” (“Solicitation includes efforts to induce a single transaction or to develop an ongoing securities business relationship. Conduct deemed by the staff to be solicitation includes telephone calls from a broker-dealer to a customer encouraging use of the broker-dealer to effect transactions, as well as advertising one’s function as a broker or a market maker…within the United States.”).
A U.S. chaperoning broker-dealer is not obligated to review and approve research reports that a foreign broker-dealer distributes directly to major U.S. institutional investors. FAQ 5 clarifies that when a foreign broker-dealer distributes research directly to major U.S. institutional investors (without the involvement of a U.S. registered broker-dealer, even if the foreign broker-dealer has a chaperoning arrangement in place), the U.S. chaperoning broker-dealer would not be required to review and approve the report, or to proactively acquire and retain a copy of the report. On the other hand, the FAQ reminds U.S. registered chaperoning broker-dealers that if they nonetheless obtain a copy of a research report that the foreign broker-dealer has distributed directly to major U.S. institutional investors (regardless of the source from which such report was obtained), the chaperoning broker-dealer should in that case retain a copy of the report in order to fulfill its chaperoning obligations under Rule 15a-6(a)(3).

Solicitation and Effecting of Transactions with and for U.S. Institutional and Major US Institutional Investors on a “Chaperoned” Basis (Rule 15a-6(a)(3)); Reliance Upon the Seven Firms and Nine Firms Letters

Rule 15a-6(a)(3) allows a foreign broker-dealer to solicit securities transactions by “U.S. institutional investors” and “major U.S. institutional investors,” provided that the foreign broker-dealer effects any resulting transactions through a U.S. registered broker-dealer (the “chaperoning broker-dealer”) and the foreign broker-dealer provides the SEC with any information or documents it may request in connection with such transactions. In addition, the foreign broker-dealer’s personnel effecting transactions with such U.S. investors must generally conduct all securities activities from outside the United States and must satisfy certain standards (e.g., they may not be subject to any statutory disqualification, as defined in Section 3(a)(39) of the Exchange Act, or any substantially equivalent foreign provisions).

The Rule requires the U.S. chaperoning broker-dealer to obtain various information from the foreign broker-dealer and its personnel, including written consent to service of process for any civil action brought by or proceeding before the SEC or a U.S. broker-dealer self-regulatory organization (“SRO”). In addition, the Rule provides that the U.S. chaperoning broker-dealer through which the transactions are effected must remain responsible for: (i) issuing all confirmations and statements; (ii) as between itself and the foreign broker-dealer, arranging or extending credit with respect to the transactions; (iii) maintaining all requisite records, including those required under Rules 17a-3 and 17a-4; (iv) complying with the net capital rule (Rule 15c3-1) with respect to any such transactions; (v) receiving, delivering, and safeguarding the U.S. investor’s funds and securities in compliance with the customer protection rule (Rule 15c3-3); and (vi) with respect to U.S. institutional investors not qualifying as major U.S. institutional investors, participating in all oral communications between the foreign broker-dealer’s personnel and the U.S. investors.

Reliance upon the 1996 Seven Firms Letter. In the Seven Firms Letter, the SEC staff indicated that it would not recommend enforcement action to the SEC if a foreign broker-dealer affiliated with a U.S. registered broker-dealer solicited and effected transactions in “foreign securities” with “U.S. resident fiduciaries” acting with discretion on behalf of “offshore clients” (in each case as those terms are defined in the letter), without the foreign broker-dealer registering with the SEC or effecting the transactions in accordance with the detailed chaperoning conditions of Rule 15a-6(a)(3). FAQ 8 expresses the SEC staff’s view that a foreign broker-dealer may rely upon the no-action position expressed in the Seven Firms Letter even if it is not affiliated with its U.S. registered “chaperoning” broker-dealer.

Reliance upon the 1997 Nine Firms Letter. In the Nine Firms Letter, the SEC staff indicated that it would not recommend enforcement action to the SEC if a U.S. affiliated foreign broker-dealer engaged in certain activities

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12 See supra note 4. 13 See supra note 4. In addition to providing a substantially expanded interpretation of the “major U.S. institutional investor” definition (as previously discussed), the Nine Firms Letter provides that: (i) in transactions involving “foreign securities” (as defined in the Seven Firms Letter) or U.S. government securities intermediated by a U.S. broker-dealer under Rule 15a-6(a)(3),
without registering with the SEC or complying with certain of the aforementioned conditions and limitations of Rule 15a-6(a)(3). As a practical matter, the Nine Firms Letter served to substantially liberalize the conditions of Rule 15a-6(a)(3) as they applied to U.S. affiliated foreign broker-dealers. As previously noted, FAQ 6 clarifies the SEC staff’s view that foreign broker-dealers not affiliated with a U.S. registered chaperoning broker-dealer may also rely upon the relief afforded in the Nine Firms Letter.

Foreign broker-dealers’ sending confirmations and account statements directly to U.S. institutional and major U.S. institutional investors. FAQ 4 indicates that a foreign broker-dealer may, to the extent required by foreign law or internal policies and procedures applicable to the firm’s global business operations, send confirmations and account statements directly to its U.S. counterparties (i.e., essentially acting on behalf of the U.S. registered chaperoning broker-dealer). The FAQ proceeds to note, however, that the U.S. registered chaperoning broker-dealer will remain responsible for ensuring that such confirmations and account statements are timely delivered and comply with all other applicable U.S. requirements, including Exchange Act Rule 10b-10 and applicable SRO rules. The FAQ also notes that any confirmation or account statement sent directly to a U.S. counterparty on behalf of a U.S. registered chaperoning broker-dealer must clearly identify the U.S. registered chaperoning broker-dealer on whose behalf the document is sent.

Net capital related obligations of U.S. registered chaperoning broker-dealers; introducing brokers as “chaperoning” brokers. FAQs 10 and 12 clarify that a U.S. registered chaperoning broker-dealer is subject to a minimum net capital requirement of at least $250,000, unless the U.S. registered chaperoning broker-dealer (which may be an “introducing broker”) has in place a fully disclosed carrying agreement with another U.S. registered broker-dealer that has agreed in writing to comply with the net capital and other financial responsibility rules with respect to the chaperoning arrangement. In this case, the chaperoning (introducing) broker-dealer would be subject to a minimum net capital requirement of at least $5,000, or such greater amount as would be required by the SEC’s net capital rule, based upon the chaperoning broker-dealer’s activities. However, a U.S. registered broker-dealer that only chaperones a foreign broker-dealer with respect to delivery-versus-payment/receipt-versus-payment (“DVP/RVP”) (direct settlement) transactions (that are directly entered into, and directly effected, between appropriate U.S. institutional investors and such foreign broker-dealer) involving foreign securities and/or U.S. government securities, as permitted under the Nine Firms Letter, would need to maintain minimum net capital of $250,000, even though the U.S. registered chaperoning broker-dealer is, in effect, acting as an introducing broker much like an M&A advisory firm under FAQ 11, as discussed below.14 FAQ 15 clarifies that a U.S. registered chaperoning broker-dealer must take a net capital clearance and settlement may occur through the direct transfer of funds and securities between a U.S. institutional or U.S. major institutional investor and a U.S. affiliated foreign broker-dealer, provided that the U.S. affiliated foreign broker-dealer: (1) is not acting as custodian of the funds or securities of the U.S. investor; (2) agrees to make available to the U.S. registered chaperoning broker-dealer clearance and settlement information relating to such transfers; and (3) is not in default to any counterparty on any material financial market transaction; and (ii) a U.S. affiliated foreign broker-dealer’s foreign personnel (i.e., its foreign associated persons) may, without the participation of an associated person of the U.S. registered chaperoning broker-dealer: (1) engage in oral communications from outside the United States with U.S. institutional investors that do not qualify as major U.S. institutional investors (even under the expanded interpretation), where such communications occur outside of the trading hours of the New York Stock Exchange, Inc., so long as the foreign associated persons do not accept orders to effect transactions other than those involving “foreign securities” (as defined in the Seven Firms Letter); and (2) have in-person contacts during visits to the United States with major U.S. institutional investors (applying the expanded interpretation), so long as the number of days on which such in-person contacts occur does not exceed 30 per year and the foreign associated persons engaged in such contacts do not accept orders to effect transactions while in the United States.

14 FINRA has, previously, only required U.S. registered chaperoning broker-dealers to maintain minimum net capital of $100,000 when acting as chaperone for delivery-versus-payment/receipt-versus-payment transactions in accordance with the Nine Firms Letter, which is generally reflected in the broker-dealer’s FINRA membership agreement. Pursuant to NASD Rule 1011(b)(3), engaging in activities that would require a FINRA member to maintain a higher minimum net capital level under Rule 15c3-1 constitutes a “material change in business operations” that would trigger a filing with, and approval by, FINRA under NASD Rule 1017(a)(5). It would appear that if such a FINRA member now increases its minimum net capital to $250,000, as required under the FAQs, such net capital increase should not be deemed by FINRA to constitute a “material change in business operations.”
charge for any failed transactions, even if the foreign broker-dealer is required to take a fails charge under foreign law, unless the chaperoning broker-dealer has entered into a fully disclosed carrying agreement with another U.S. registered broker-dealer in accordance with the conditions and circumstances described in FAQ 10 (in which case the carrying broker-dealer would have to take a net capital charge for any failed transactions), even with respect to delivery-versus-payment/receipt-versus-payment transactions in foreign securities and U.S. government securities, as described above.

FAQs 13 and 14 emphasize that a U.S. registered broker-dealer maintaining a minimum net capital of only $100,000 pursuant to Rule 15c3-1(a)(2)(i), for broker-dealers relying upon the Rule 15c3-3(k)(2)(i) exemption, may not act as the Rule 15a-6(a)(3) chaperone for a foreign broker-dealer, even in the case of DVP/RVP transactions with institutional investors.

FAQ 11 sets forth the staff’s view that if a foreign broker-dealer’s business under Rule 15a-6(a)(3) is limited to M&A advisory services to a U.S. institutional or major U.S. institutional investor contemplating the acquisition of a company, the U.S. registered chaperoning broker-dealer would, by virtue of this activity alone, be subject to a minimum net capital requirement of at least $5,000.15 It should follow that a U.S. registered chaperoning broker-dealer that only chaperones a foreign broker-dealer in connection with private placements of securities pursuant to Section 4(a)(2) of the Securities Act of 1933, and/or Rule 506 of Regulation D thereunder, should only need to maintain minimum net capital of $5,000, although this was not specifically addressed by the SEC.

Recordkeeping obligations of U.S. registered chaperoning broker-dealers. FAQ 15 notes that the existence of a carrying agreement does not relieve a U.S. registered chaperoning (introducing) broker-dealer of its recordkeeping obligations with respect to open trades and failed transactions. In addition, FAQ 16 reminds U.S. registered chaperoning broker-dealers that they remain responsible for complying with required books and records obligations relating to securities transactions, including those required by Rules 17a-3 and 17a-4 under the Exchange Act, and must make and retain accurate records reflecting the trades between the U.S. investors and the foreign broker-dealer.16

Solicitation and Effecting Transactions with and for Certain Exempted Parties (Rule 15a-6(a)(4))

Rule 15a-6(a)(4) permits a foreign broker or dealer to solicit certain exempted parties, and to effect transactions with or for such parties, without regard to the chaperoning and intermediation requirements that would be otherwise required under paragraph (a)(3) of the Rule. These persons include, among others, foreign persons temporarily present in the United States with whom the foreign broker or dealer has a bona fide, pre-existing relationship before such person came to the United States.

FAQ 1 notes that while the determination of whether a foreign person is only “temporarily present” in the United States remains facts and circumstances specific, a foreign person that is not otherwise deemed a “resident” of the United States under applicable law would be presumed to be only “temporarily present” in the United States for purposes of Rule 15a-6(a)(4)(iii). The FAQ goes on to state the SEC staff’s belief that a foreign broker-dealer may effect transactions with a foreign person located in the United States with whom the foreign broker-dealer had a bona fide, pre-existing relationship before such person came to the United States, so long as such foreign person: (i) is not a U.S. citizen; and (ii) is not a lawful permanent resident of the United States (i.e., a “Green Card holder”).

15 See also E&Y Letter, supra note 8, for additional relief relating to the application of Rule 15a-6(a)(3) to cross-border M&A activities.

16 See also Letter re: Morgan Stanley India Securities Pvt. Ltd., SEC No-Action Letter, 1996 SEC No-Act. LEXIS 975 (December 20, 1996) (allowing a U.S. registered chaperoning broker-dealer to comply with the books and records chaperoning requirement of Rule 15a-6(a)(3)(iii)(A)(4) by having access to required trade records maintained by a regulated foreign broker-dealer/affiliate through a linked computer system as soon as such records are created (but which records would not be transferred to or maintained by the U.S. broker-dealer).
Relationship to Other Exchange Act and State-Level Registration Requirements

It should be noted that Rule 15a-6 is merely an exemption from registration as a “broker” or “dealer” pursuant to Section 15(a)(1) of the Exchange Act, as those terms are defined in Sections 3(a)(4) and 3(a)(5), respectively, under the Exchange Act. As such, Rule 15a-6 would not provide an exemption with respect to a foreign entity that engages in activities as a “security-based swap dealer” under the Exchange Act (an “SBSD”), as an SBSD is excluded from the definition of “dealer” in Section 3(a)(5) (assuming that the SBSD is not otherwise effecting transactions in security-based swaps as a “broker”). In addition, Rule 15a-6 has no impact on applicable broker-dealer registration requirements under the various States’ Blue Sky laws, although most, but not all, States do not require such registration with respect to transactions involving certain categories of institutional investors in such States.

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