

Client Alert

A report
for clients
and friends
of the Firm

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SEC and Federal Reserve Board Issue Final “Push-out” Rules

The SEC and Federal Reserve Board recently adopted a single set of final rules that implement certain of the exceptions for banks from the definitions of “broker” and “dealer” under the Securities Exchange Act of 1934. These final rules do not effect a material change to provisions applicable to existing custodial and non-custodial securities lending activities of banks.

Currently, banks are permitted to effect securities lending or borrowing transactions with or on behalf of customers in connection with the provision of custodial services or investing cash collateral pledged in connection with such transactions. By rule, the SEC had expanded permitted bank activities (not subject to push-out) to cover riskless principal securities lending and non-custodial securities lending agency transactions.

A new Rule 772 to Regulation R has been adopted which allows non-custodial securities lending agency activities to occur within the bank so long as such securities lending activities are with or on behalf of a person whom the bank reasonably believes to be a “qualified investor” (as defined in Section 3(a)(54)(A) of the Securities Exchange Act) or any employee benefit plan that owns and invests on a discretionary basis not less than \$25 million in investments. The dealer provisions of former Rule 15(a)-11 have been recodified as a new Rule 3a5-3, which continues the exemption of banks from the definition of dealer for purposes of conduit securities lending transactions (in which the bank acts as principal to borrow and re-lend securities) to “qualified investors” or employee benefit plans of the requisite investment asset size.

Interestingly, although requested, the SEC and Federal Reserve Board declined to exempt repurchase and reverse repurchase transaction in non-exempt securities from the

“broker” and “dealer” definitions, notwithstanding that such repo activities are generally viewed as functionally similar to securities lending. The agencies deferred consideration of this matter and invited comment on the following issues: (1) the nature, structure (including term and type of security involved), and purpose of repurchase and reverse repurchase agreements currently conducted with respect to non-exempt securities; (2) the types of customers and financial institutions currently involved in repurchase and reverse repurchase agreements with respect to non-exempt securities; (3) the extent to and manner in which banks currently engage, as agent or principal, in repurchase and reverse repurchase agreements with respect to non-exempt securities; (4) recent developments or trends in the market for repurchase and reverse repurchase agreements with respect to non-exempt securities; (5) any material similarities or differences in the use, structure, customer base, or legal, regulatory, tax or accounting treatment of repurchase and reverse repurchase agreements with respect to non-exempt securities, on the one hand, and repurchase or reverse repurchase agreements with respect to exempt securities or securities lending transactions involving exempt or non-exempt securities.

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