

SEC Seriously Limits Dealer/Trader Distinction: Betting Window Open Re Federal Court Veto

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On February 6, 2024, the SEC adopted new rules under the Securities Exchange Act of 1934 (Exchange Act), to expand the scope of “dealers” and “government securities dealers” required to register under the Exchange Act, become members of FINRA, and comply with the federal securities laws and FINRA regulatory obligations. Historically, Section 3(a)(5) of the Exchange Act has excluded traders from the definition of “dealer” unless trading was done “as a part of a regular business.” Under the new rules, a person buying and selling securities for its own account could be deemed to do so “as part of a regular business” if that person engages in a regular pattern of buying and selling securities that has the effect of providing liquidity to other market participants. For more detailed information about the background and effects of the new rules, see [“SEC Wants More Securities Traders Under Its Dealer Big Top, Would Require Exchange Act Registration by More Regular Traders,”](#) *Expect Focus – Life, Annuity, and Retirement Solutions* (January 2024).

By thus narrowing the trader exemption, the new rules turn many traders into dealers, subjecting them to costly broker-dealer regulation and requiring significant operational changes. While the express purpose of the new rules is to regulate market participants that play a “significant liquidity-providing role in overall trading and market activity,” the impact of the new rules may extend beyond the intended purpose. Market participants potentially covered by the new rules include proprietary trading firms that trade for their own account, also known as high-frequency trading firms, private investment funds, pension funds, and collective trust funds. However, registered investment companies and persons that have or control less than \$50 million in total assets are excluded. The SEC vote on the new rules was split 3–2. The dissenters, Commissioners Mark T. Uyeda and Hester M. Peirce, expressed concern about SEC overreach of claimed jurisdiction and creation of regulatory confusion. Three trade associations for the private fund industry promptly filed a lawsuit against the SEC, asking a federal court to scrap the new dealer definition as arbitrary, capricious, and outside the

agency's statutory authority to enact. Among other things, they say the SEC's estimate that the new rules would require fewer than 16 private funds to register as dealers "has no basis in the record" and "is wrong." The rules became effective on April 29, 2024, and the compliance date is one year from that effective date.

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