

# Regulatory Alert

Regulatory Insights for Financial Services

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## Swaps: SEC Examinations Risk Alert; CFTC Proposals

### KPMG Insights:

- **Supervisory Insights:** SEC and CFTC each focus attention on reporting, recordkeeping, and risk management. Swaps are among the SEC's 2024 examination priorities.
- **Data Focus:** Accurate, timely, complete, and high-quality data related to swaps activity to support transparency in the swaps markets.
- **Strong Controls:** SEC Risk Alert and CFTC proposals stress strong controls to promote accuracy and to prevent, detect, and mitigate identified risks.

### SEC Risk Alert

The Securities and Exchange Commission (SEC) Division of Examinations (Division) issues a [Risk Alert](#) in which it shares observations, based on examinations and outreach, related to security-based swap dealers' compliance with relevant rules and requirements under the Securities Exchange Act of 1934 (Exchange Act). The Division aims to remind security-based swap dealers of their obligations under the relevant rules and encourage them to consider improvements in their compliance programs, policies, procedures, and internal controls.

The Division states that, in general, some security-based swap dealers did not "establish, maintain, or enforce reasonably designed policies and procedures addressing applicable Exchange Act requirements" while some did not comply with these requirements, including Regulation SBSR (which "governs the regulatory reporting and public dissemination of security-based swap transactions and requires market participants to report security-based swap information to a registered security-based swap data repository"). Observations

concerning four specific areas were highlighted by the Division:

1. Reporting of security-based swap transactions and correction of reporting errors
2. Business conduct standards
3. Security-based swap trading relationship documentation and portfolio reconciliation
4. Recordkeeping

### 1. Reporting of Security-Based Swap Transactions and Correction of Reporting Errors:

The Division observed that some dealers failed to report certain security-based swap trade data within the required timeframes or to accurately report trade information. Examples include reporting inaccurate notional amounts, misreporting underlying asset information, and failing to adequately report counterparty identifications. The Division also noted that "in many instances", these failures were related to weak internal controls and processes for ensuring accurate reporting, and that some securities-based swap dealers lacked procedures to identify and correct reporting errors.

**2. Business Conduct Standards:** The Division identified several issues related to security-based swap dealers' compliance with business conduct standards (Exchange Act Rule 15Fh-3(h)) as well as some security-based swap dealers that did not establish a system to address the minimum requirements, including procedures to:

- Prohibit a supervisor from supervising his or her own activities.
- Prevent negative impacts from conflicts of interest (i.e., identify, manage, mitigate).
- Facilitate supervisory review of external correspondence with counterparties and internal communications related to the securities-based swap dealer's business.
- Review associated persons' trading relationships or activities.
- Conduct an internal business review, at least annually, to detect and prevent violations of applicable securities laws, rules, and regulations.

**3. Security-Based Swap Trading Relationship Documentation and Portfolio Reconciliation:**

"Exchange Act Rule 15Fi-5 requires each security-based swap dealer to establish, maintain, and follow written policies and procedures reasonably designed to ensure the execution of written security-based swap trading relationship documentation with each counterparty that complies with the requirements of the Rule." The Division observed that some dealers did not:

- Have independent auditors perform periodic audits of trading relationship documentation policies and procedures.
- Retain records of a senior officer's written approval of trading relationship documentation policies and procedures, and related amendments.
- Agree in writing on portfolio reconciliation terms with counterparties.

**4. Recordkeeping:** The Division found that certain dealers did not consistently maintain complete and accurate records as required under the Exchange Act

Rules 17a-3 and 18a-5. Examples included incomplete or inaccurate trade blotters, counterparty listings, and associated person listings.

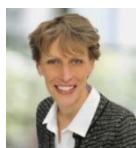
**CFTC Rule Proposals**

The Commodity Futures Trading Commission (CFTC) separately proposes rules applicable to CFTC-supervised Swap Dealers (SDs) and Major Swap Participants (MSPs), including proposals to:

- Revise CFTC regulations regarding [real-time public reporting](#) and swap data recordkeeping and reporting. The proposed amendments would allow a unique product identifier (UPI) and product classification system to be implemented for the Other Commodity asset class, as well as modify certain data elements to increase data quality, accuracy, and standardization. Comments are requested no later than February 26, 2024. The proposal follows a February 2023 CFTC order, which designated a UPI for use in swap recordkeeping and data reporting for the Interest Rate, Credit, Foreign Exchange, and Equity asset classes.
- Require SDs, MSPs, and futures commission merchants to "establish, document, implement, and maintain an [Operational Resilience Framework](#) reasonably designed to identify, monitor, manage, and assess risks relating to information and technology security, third-party relationships, and emergencies or other significant disruptions to normal business operations." Comments are requested by March 2, 2024.
- Amend the [capital and financial reporting](#) requirements of SDs and MSPs by codifying certain staff interpretations and revising certain regulations to make it easier for SDs and MSPs to comply with the CFTC's financial reporting obligations and demonstrate compliance with minimum capital requirements. Comments are requested no later than February 13, 2024.

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