Insights into recent SBSD and SD examinations

KPMG

Exam regulatory priorities

KPMG LLP (KPMG) has assisted swap dealers (SDs) and security-based swap dealers (SBSDs) with their National Futures Association (NFA) and Securities and Exchange Commission (SEC) examinations, through which we have identified common compliance challenges, solutions, and industry insights.

Key takeaways

- The SEC is well into its first cycle of examinations of SBSDs.
- In advising our clients, we note that the SEC's approach to SBSD examination has been markedly different than the approach employed by the NFA to examine Commodity Futures Trading Commission (CFTC) registered swap dealers. Specifically:
  - **Scope** – SEC examinations are generally full scope, whereas NFA began its examinations of SDs by reviewing more discrete areas of rules (e.g., risk management program)
  - **Duration** – The duration of SEC examinations is generally longer than NFA examinations, with one client's examination lasting nearly a year and a half.
  - **Knowledge** – SEC examiners are still coming up the curve of market practices, which means that SBSDs must communicate clearly how they comply with relevant regulations.
- **SEC has also begun to look behind substituted compliance**, asking SBSD management how they know they are in compliance with relevant home country regulations. It remains to be seen whether NFA follows suit with SDs.
- Required reviews – Lastly, SEC has inquired about SBSDs' practices for undertaking independent reviews required by regulation. For ease of reference, we list these required reviews for both SDs and SBSDs on the next page.

Shared regulatory focus areas:

- Surveillance/ Supervision (trade and communication)
- Recordkeeping
- Trade reporting
- Business conduct standards
- Margin

	SEC exam overview	NFA exam overview
Duration	**10 or more months**, depending on firm size/activities	**Three to six months**, depending on firm size/activities, two weeks of on-site examination
Requests	Issued in **large batches with a two-week response time**	Issued **daily with a 72-hour turnaround**
Response timeframes	**Two-week response**	**72-hour response,** can be shorter in certain instances
Recent focus areas	**In addition to shared focus areas:** • CCO reporting lines • AP identification process • Substituted compliance • Internal audit independence • Portfolio reconciliation • Daily mark disclosures • Back testing results • SBS valuation disputes	**In addition to shared focus areas:** • AP training • Capital requirements • Risk management • Data accuracy
On-site presence	**Limited on-site**, mainly remote communication	**Regularly on-site**, detailed agendas
Regulator knowledge	More explanation required from firms on market practices and compliance processes	Expertise built on past cycles of examinations
Transparency	Limited transparency on potential findings ahead of examination report	Early insights into findings and severity

Required SD and SBSD reviews

The CFTC and SEC require SDs and SBSDs to conduct periodic reviews, as shown in the table below. We advise our clients to use these reviews to proactively identify areas of noncompliance ahead of regulatory examinations.

Swap Dealers

B.C.D.R. (Annual and Triennial)
17 C.F.R. § 23.603(g)

The CFTC requires annual (internal) and triennial (external) reviews of SDs' business continuity and disaster recovery plans to ensure effectiveness and regulatory compliance, enhancing resilience and operational readiness.

Information System Security Program Review (Annual)
NFA Interpretive Notice 9070

The NFA requires SDs to perform regular reviews of their ISSPs at least once every 12 months using either in-house staff with appropriate knowledge or by engaging an independent third-party information security specialist.

Initial Margin Reviews (Annual)
17 C.F.R. § 23.154(b);
12 C.F.R. § 45.8(f)

SDs are required to at least annually review their IM models. In addition, SDs must annually audit the controls for calculating, collecting, and monitoring initial margin, with a report delivered to the governing body, senior management, and the CCO.

Trading Relationship Documentation Audit (Periodic)
17 C.F.R. § 23.504(c);
17 C.F.R. § 240.15Fi-5(c)

SDs and SBSDs are required to have an independent auditor conduct periodic audits to identify any material weakness in documentation policies and procedures. The audits should review onboarding documentation collection, review, and retention processes and controls designed to maintain accurate and complete trading documentation with counterparties.

Capital Financial Reports (Annual)
17 C.F.R. § 23.105(e);
17 C.F.R. § 240.18a-7

SDs and SBSDs are required to submit audited financial statements as part of the capital requirements. These audited filings consist of financial condition statements, income and cash flow statements, changes in equity and liabilities, footnote disclosures, regulatory capital compliance, reconciliation of material differences from unaudited reports, and any additional necessary information to ensure accuracy and clarity.

RMP and Position Limits (Annual and Periodic)
17 C.F.R. § 23.600(e);
17 C.F.R. 23.601(h);
17 C.F.R. § 240.15c3-4(c)

SDs are required to at least annually review and test the Risk Management Program (RMP), including its compliance with position limit requirements under 23.601.

SBSDs are required to conduct periodic reviews (which may be performed by internal audit staff) and annual reviews (which must be conducted by independent certified public accountants) of the RMP.

SBSDs

Securities Counts (Quarterly)
17 C.F.R. § 240.18a-9(a)

This rule mandates that all securities held or controlled (but not physically possessed for 30 or more days) by a SBSD be examined and reconciled with books and records by personnel who do not have direct responsibility for the care and protection of securities.

Supervisory Review (Annual)
17 C.F.R. § 240.15Fh-3(h)

The SEC requires SBSDs to at least annually review the security-based swap business to determine whether the compliance program is reasonably designed to assist in detecting and preventing violations of applicable federal securities laws and the rules and regulations thereunder.

VaR Model Reviews (Annual and Periodic)
17 C.F.R. § 240.18a-1

The SEC requires periodic and annual (latter of which must be conducted by a registered public accounting firm) reviews of Value-at-Risk (VaR) models utilized by security-based swap dealers and required by regulators.

How KPMG can help

Our team of former regulators and industry veterans understands SEC and CFTC expectations and leading industry practices. Discover how our reviews, grounded in deep knowledge and practical experience, provide substantial value in navigating an increasingly complex regulatory landscape.

Our team

Mike Sullivan
Principal, Markets Compliance
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Mike leverages deep industry experience to help SDs meet complex regulatory requirements. His achievements include assisting a SEF with CFTC reporting compliance and guiding a Futures Commission Merchant through regulations on capital modeling and risk management.

Stefan Cooper
Principal, Markets Compliance
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With extensive experience in operational reviews for global financial institutions, Stefan excels in enhancing regulatory frameworks for SDs. Key accomplishments include leading regulatory reporting reviews and assisting with CFTC and SEC registrations to help ensure compliance.

Conway Dodge
Principal, Markets Compliance
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Conway brings exceptional regulatory experience to SDs. With a distinguished 12-year tenure at the SEC, Conway excels in navigating complex compliance landscapes, involving both civil and criminal investigations, and coordinating with international regulatory bodies.

DJ Hennes
Managing Director, Markets Compliance
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DJ advises CFTC and SEC registrants on governance, supervision, and compliance issues. He has past experience with registration, assessments, and enforcement matters. Prior to joining KPMG, DJ spent 15 years at Promontory Financial Group, where he led the capital markets practice for the Americas.
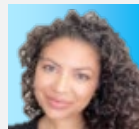
Jennifer Estremera
Director, Markets Compliance
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Experienced in SD compliance, Jennifer has managed CFTC SD registrations and developed compliance manuals to help ensure regulatory adherence. Prior to joining KPMG, Jennifer worked in-house at major banking organizations' operations, compliance, and legal functions.
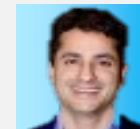
Rafe Kausar
Manager, Markets Compliance
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Rafe joined KPMG from the NFA, where he examined SD registrants. He has conducted risk-based examinations focusing on market conduct, trade reporting, and risk management. Since joining KPMG, he has advised SEFs, SDs, and SBSDs, including supporting a Top 20 bank through the NFA SD registration process.

Revolutionize trade reporting reviews with AI insights

Contextualization

Our AI-enhanced tool can provide context for the testing results, relating observed errors and issues to specific aspects of the client's trade reporting program and the relevant regulatory requirements.

Validation

Employ our AI-enhanced toolkit to compare data points submitted to the CFTC with the original data from source systems, helping ensure accuracy and completeness of the submitted reports.

Data analysis

As part of testing, our AI-enhanced toolkit can process and analyze large volumes of trade reporting data, identifying patterns, discrepancies, and potential compliance issues efficiently and accurately.

Summarization

AI can enhance our testing by generating concise, human-readable summaries of the testing results, highlighting key findings, trends, and areas of concern to facilitate effective communication with stakeholders.

Logic evaluation

Utilize AI-enhanced tools to evaluate reporting logic, identifying any inconsistencies, inefficiencies, or gaps that could lead to inaccurate or incomplete reporting, and thus impact compliance with CFTC requirements.

In the rapidly evolving regulatory landscape, maintaining accuracy and compliance in trade reporting is more critical than ever. KPMG goes beyond traditional trade reporting reviews, offering innovative AI-supported testing and review services for your trade reporting programs. As areas under close scrutiny by the CFTC and NFA, the accuracy and comprehensiveness of these reports are paramount.

Leveraging the power of AI, our approach not only identifies compliance gaps but also anticipates potential areas of concern, helping ensure your trade reporting processes are both efficient and ahead of regulatory curves.

With our AI capabilities, you can transform your trade reporting from a regulatory requirement to a regulatory advantage.
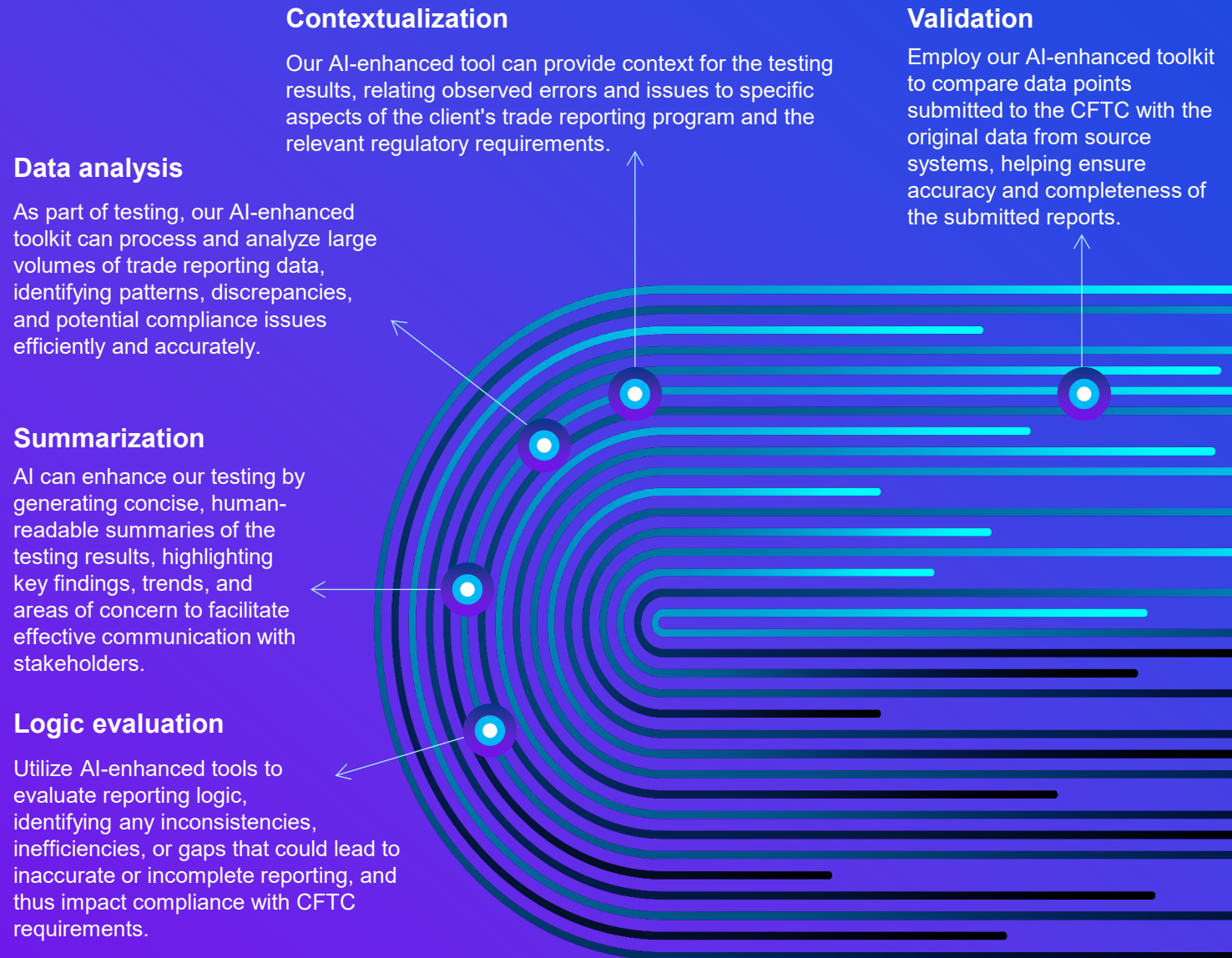
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MADE | MDE200653 (February 2025)