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Sent: Thursday, February 07, 2019 10:33 AM
To: Macchiaroli, Michael A.; McGowan, Thomas K.; Roy, Randall W.; Thomas J. Smith)
Cc: Deng, Valentina; Fox, Timothy C.; Lombardo, Raymond A.; Scucci, Mary Kay
Subject: Audit Requirements for Security Based Swap Dealers (SBSD) and Swap Dealers (SD)

Mike, Tom, Randall and Tom:

I am sending you this e-mail as an “informal comment letter” from SIFMA based upon conversations the industry has had with the SEC and the CFTC regarding audit requirements for Security Based Swap Dealers (SBSDs) and Swap Dealers (SDs)

Request for US GAAS audits for all SBSBs

Conceptually, what the industry is advocating for is that the SEC’s final swap rules not require PCAOB audits of all SBSB, but rather require “regular GAAS audits” for the financial statements and the related supplemental schedules. The industry is also strongly requesting that the final SBSB rule specifically excludes “other reports” from 17a-5 (and 15c3-3?) so that PCAOB requirements for any reports that the Commission may request in their final rule are not inadvertently scoped in and become subject to PCAOB requirements (i.e., AT1 and AT2). SIFMA will be making this same request for “regular GAAS audits” and “other reports” exclusion from the CFTC for their Swap Dealers (SDs).

The reason we are proposing this approach is because:

1. This approach will provide the most consistent audit approach for the entire swap market for all regulators (i.e., SEC, CFTC, Fed/FDIC/OCC).
2. This will provide a path to harmonization with the CFTC for jointly registered entities and provide the same audit standards for both SEC and CFTC stand-alone entities.
3. The audit procedures between PCOAB and the GAAS are almost identical and GAAS is currently used within the industry by other regulators.
4. The audit work done on supplemental schedules under PCOAB AS 17 will be retained under a GAAS audit under AU 551.
5. Specifically exclusion of “other reports” will assure that any swap “other reports” will not be inadvertently scoped in and then subject to the PCAOB requirements AT1 and AT2. This is especially important as we believe the SEC’s “other reports” may include detailed data requirements that are not in the industry’s financial reporting systems. The industry is not advocating that we don’t provide the Commission with the data, we are just asking to assure that is it not inadvertently subject to PCAOB examination requirements.
6. Other than not requiring audits at all, this approach will be the lowest cost alternative and will provide the Commission the same benefits as a PCOAB audit.

To help illustrate our proposal I have attached a file listing the different legal entity configurations of SBSBs, SDs and Banking swap entities so that you can see the harmonization that our proposal will bring under this approach and the related audit standards. (**See File: Swap Reports and Audit Exam Applications FINAL Feb 7 2019**).

We are proposing this approach and will be asking the CFTC to use the same approach so that there is consistency (as much as possible) between BDs, FCMs, SBSBs and SDs. Obviously, we cannot harmonize completely between the SEC and the CFTC (due to existing regulations) but our proposal provides the next best alternative. Additionally, this approach will avoid all of the surprises and additional costs the industry experienced with Broker-Dealer Reports (17a-5). I have copied the CFTC on this proposal so that they are aware of what we are proposing.

Elimination of PCAOB requirements (AT1 and AT2) for Compliance and Exemption Reports

Mike, since we believe the Commission may be working to comply with the Presidential Executive Order on Reducing Regulation and Controlling Regulatory Costs (issued on January 30, 2017) the industry has a suggestion to help comply with this Executive Order. Since you will be issuing reporting requirements for swap dealers, we suggest that you use this as an opportunity to correct the erratum in Broker Dealer Reports (i.e., 17a-5) that subjects the Exemption and Compliance Reports to PCAOB AT1 and AT2. As you know the regulatory intent of your regulations for reporting for Broker Dealers was supposed to be focused on the Commissions Financial Responsibility Rules but what it inadvertently did was expand the role of the PCAOB.

I had quantified some industry data in 2015 for the first year of the PCAOB audited Compliance Report. The report had been filed by approximately 200 firms and that during the first year of 17a-5 and we believe that there was no real “new” regulatory information from the Compliance Report. That initial year approximately 10-20 firms had in issues as identified by the report, typically for either holding on to checks or for a 15c3-3 Reserve Accounting calculation errors. However, at that time the SEC was already aware of these violations as the firms had filed either a 17a-11; Notification Provision for Brokers and Dealers, or a 15c3-3(i) Notification in the event of failure to make a required deposit. With this report obviously providing a non-existent benefit to the Commission we believe that you would be able to eliminate the PCAOB examination requirements (i.e., AT1 and At2) as there are existing SEC regulations and SEC/FINRA examinations that already provide this regulatory and compliance benefit.

The industry is not proposing the elimination of the compliance or the exemption report as we respect the Commissions desire for this information, but we do suggest the removal of the PCAOB examination requirements (i.e., AT1 and AT2) for these reports, as we believe they provide no regulatory value in light of the Commissions other regulations. The removal would reduce regulatory cost on the broker dealer and reduce stress in the system. However, understand I am making this suggestion based upon the limited data I generated in 2015 and subsequent antidotal information. (Note: If you do decide to eliminate the AT1 and AT2 requirement please also remember the interaction with the investment management division and Rule 206.)

I hope my attached chart and this note provide you with the information you need to harmonize the swap audit standards. If you have any additional questions or need additional information on the swap audit proposal, please feel free to give me a call.

Regards,

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Swap Reports and Audit Exam Requirements

SIFMA Proposal (in Red)

Type of Entity	Audit Requirement for Traditional Finance Statements*	Supplemental Schedules	Other Reports	Comment
BD/FCM/SBSD/SD	<p>BD – FOCUS PCOAB Audit</p> <p>FCM – 1FR PCOAB and GAAS Audit</p> <p>SBSD – GAAS Audit</p> <p>SD – GAAS Audit</p>	<p>BD – Calculations for 3-1, 3-3 including PAB (AS 17)</p> <p>FCM - Net capital, seg, secured sequestered, stmt of cleared swaps (AS 17)</p> <p>SBSD – AU 551 (GAAS equivalent to AS 17)</p> <p>SD - AU 551 (GAAS equivalent to AS 17)</p>	<p>BD - Compliance & Exemption (PCAOB AT1 and AT2) *</p> <p>FCM - MI</p>	<p>BD - Reports in 17a-5 as part of the FRR creating the AT1, AT2 requirement.</p> <p>SBSD - Need to specifically exclude Other Reports from FRR under 17a-5 (and 15c3-3?) or they will be scoped into AT1, AT2</p> <p>SD – Need to specifically exclude Other Reports from 1.16 or it will be scoped into the MI letter</p>
BD Lite/SBSD	<p>SBSD – GAAS Audit</p> <p>SD – GAAS Audit</p>	<p>SBSD – AU 551</p> <p>SD – AU 551</p>		
SBSD Stand Alone	<p>SBSD – GAAS Audit</p> <p>SD – GAAS Audit</p>	<p>SBSD – AU 551</p> <p>SD – AU 551</p>		
SD Stand Alone	<p>SBSD – GAAS Audit</p> <p>SD – GAAS Audit</p>	<p>SBSD – AU 551</p> <p>SD – AU 551</p>		
SBSD/SD	<p>SBSD – GAAS Audit</p> <p>SD – GAAS Audit</p>	<p>SBSD – AU 551</p> <p>SD – AU 551</p>		
Banking Swap Entities	GAAS Audit	AU 551	FRY9-C and Call Report not audited.	

*Traditional Financial statement such as income statement, balance sheet and footnotes.