

**MEMO# 28081**

May 1, 2014

# **SEC Proposes Recordkeeping and Reporting Requirements for Security-Based Swap Dealers, Major Security-Based Swap Participants, and Broker-Dealers**

[28081]

May 1, 2014

TO: CLOSED-END INVESTMENT COMPANY MEMBERS No. 16-14  
DERIVATIVES MARKETS ADVISORY COMMITTEE No. 31-14  
INVESTMENT ADVISER MEMBERS No. 16-14  
SEC RULES MEMBERS No. 16-14 RE: SEC PROPOSES RECORDKEEPING AND REPORTING REQUIREMENTS FOR SECURITY-BASED SWAP DEALERS, MAJOR SECURITY-BASED SWAP PARTICIPANTS, AND BROKER-DEALERS

Recently, the Securities and Exchange Commission (“SEC” or “Commission”) proposed recordkeeping, reporting and notification requirements applicable to security-based (“SB”) swap dealers and major SB swap participants and additional recordkeeping requirements applicable to broker-dealers for their SB swap and swap activities. [\[1\]](#) The Commission is proposing rule amendments to establish a recordkeeping, reporting, and notification program for broker-dealer SB swap dealers (“SBSDs”) and broker-dealer major SB swap participants (“MSBSPs”) and proposing new rules to establish a recordkeeping, reporting, and notification program for stand-alone SBSDs, stand-alone MSBSPs, bank SBSDs, and bank MSBSPs. The Proposal is modeled on the broker-dealer recordkeeping and reporting rules, and the new FOCUS Report Form SBS (“Form SBS”) is based on the Financial and Operational Combined Uniform Single Report (“FOCUS Report”). The Commission also proposes to establish notification requirements applicable to SBSDs and MSBSPs for the timely notification to the Commission of information about potential problems at the registrants.

Generally, the proposed new rules for stand-alone SBSDs and stand alone MSBSPs are narrower in scope than those applicable to broker-dealer SBSDs and broker-dealer MSBSPs to reflect the narrower range of activities engaged in by stand-alone SBSDs and stand alone MSBSPs. In addition, the proposed requirements applicable to bank SBSDs and bank

MSBSPs are narrower in scope than those applicable to stand-alone SBSs and stand-alone MSBSPs, in part, because these registrants are subject to existing recordkeeping and reporting requirements administered by prudential regulators. Comments on the Proposal are due by July 1.

This memorandum briefly describes the proposed reporting and notification requirements for SBSs and MSBSPs.

## Reporting Requirements

The Commission is proposing to establish a reporting program for SBSs and MSBSPs that is based on the reporting program for broker-dealers. Generally, SBSs and MSBSPs will be required to file periodic unaudited reports containing information about their financial and operational conditions on Form SBS and file annually financial statements and certain reports and a report covering the financial statements and reports prepared by an independent public accountant registered with the Public Company Accounting Oversight Board ("PCAOB") in accordance with PCAOB standards.

### Proposed Form SBS

The Commission is proposing new Form SBS, which would be used by all types of SBSs and MSBSPs to report financial and operational information. Broker-dealer SBSs, broker-dealer MSBSPs, stand-alone SBSs, and stand-alone MSBSPs would be required to file proposed Form SBS on a monthly basis. Bank SBSs and bank MSBSPs would be required to file proposed Form SBS quarterly. Proposed Form SBS is divided into five parts, which would apply to different types of SBSs and MSBSPs.

Part 1 of proposed Form SBS would require, among other things, the following information: (1) a statement of financial condition; (2) a computation of net capital; (3) a computation of minimum net capital required; (4) a statement of income (loss); (5) a statement of capital withdrawals, a statement of changes in ownership equity, and a statement of changes in liabilities subordinated to claims of creditors; (6) certain financial and operational data; (7) a customer reserve account computation; (8) information for possession or control requirements; (9) a computation for the determination of reserve requirements for proprietary accounts of broker-dealers; and (10) a computation of tangible net worth. [\[2\]](#)

Part 2 of proposed Form SBS would require the following: (1) a balance sheet; (2) a statement of regulatory capital; (3) an income statement; (4) a reserve account computation and (5) information for possession or control requirements. [\[3\]](#)

Part 3 of Proposed Form SBS would require sections showing: (1) a statement of segregation requirements and funds in segregation for customers trading on U.S. commodity exchanges; (2) a statement of segregation requirements and funds in segregation for customers' dealer options account; (3) a statement of secured amounts and funds held in separate accounts for foreign futures and foreign options customers; (4) a statement of secured amounts and funds held in separate accounts for foreign futures and foreign options customers; (5) a computation of the firm's minimum capital requirement; and (5) a statement of segregation requirements and funds in cleared swap customer accounts. [\[4\]](#)

Part 4 of the proposed Form SBS consists of four schedules that elicit detailed information about a firm's SB swap and swap positions, counterparties and exposures. [\[5\]](#) Part 5 consists of one schedule that is a truncated version of Schedule 1 to Part 4 of proposed

## **Annual Audited Financial Reports and Other Reports**

### **Customer Statements**

The Commission is proposing to include a customer statement requirement that is parallel to the requirement currently imposed on broker-dealers. The proposed rule, however, would require (rather than make optional as is the case with broker-dealers) website disclosure of the mandated information for stand-alone SBSDs and stand-alone MSBSPs. Specifically, stand-alone SBSDs and stand-alone MSBSPs would be required to disclose on their internet websites an audited statement of financial condition with appropriate notes within ten business days after the date the firm is required to file its audited annual reports with the Commission. In addition, a stand-alone SBSD would be required to disclose on its internet website at the same time: (1) a statement of the amount of the firm's net capital and required net capital and other information, if applicable, related to the firm's net capital and (2) if, in connection with the firm's most recent annual reports, the report of the independent public accountant identifies one or more material weaknesses, a copy of the report. In addition, stand-alone SBSDs and stand-alone MSBSPs would be required to disclose on their websites an unaudited statement of financial condition as of a date that is six months after the date of the most recent audited annual reports. Finally, stand-alone SBSDs and stand-alone MSBSPs would be required to make the information required to be disclosed to customers on their websites available in writing upon request of a customer and maintain a toll-free number to receive such requests.

### **Annual Reports**

Under the Proposal, broker-dealer SBSDs, stand-alone SBSDs, broker-dealer MSBSPs, and stand-alone MSBSPs would be required to file with the Commission each year annual reports consisting of a financial report and a compliance report as well as reports that are prepared by an independent public accountant registered with the PCAOB covering the financial report and the compliance report in accordance with standards of the PCAOB. The financial report must contain financial statements including, among others, a statement of financial condition, a statement of income, and a statement of cash flows. The financial report also must contain supporting schedules consisting of a computation of net capital, a computation of the reserve requirements, and information relating to the possession or control requirements.

## **Notification Programs**

The Commission is proposing to require the timely notification to the Commission of information about potential problems at SBSDs and MSBSPs. The proposed notification requirements for bank SBSDs and bank MSBSPs are substantially narrower in scope than the requirements for other types of SBSDs and MSBSPs.

The Proposal would require broker-dealer SBSDs and stand-alone SBSDs to notify the Commission if the firm's net capital or, if applicable, tentative net capital declines below the minimum amount required on the same day they discover or are notified of the net capital deficiency. The notice must specify the net capital or tentative net capital requirement and the current amount of net capital. A stand-alone MSBSP would be required to give notice to the Commission on the same day if it fails to maintain a positive tangible net worth or if the Commission informs the stand-alone MSBSP that it has failed to maintain position tangible

net worth. The notice would need to specify the extent to which the firm has failed to maintain positive tangible net worth.

The Proposal also requires broker-dealer SBSBs, stand-alone SBSBs, broker-dealer MSBs, and stand-alone MSBs to send notice promptly (within 24 hours) if certain events are triggered to provide the Commission with “early warning” that the registrant may experience financial difficulty. The Commission proposes to require a bank SBSD or a bank MSBS to give notice to the Commission when it files an adjustment of reported capital category with its prudential regulator by transmitting a copy of the notice to the Commission. [7]

In addition, all SBSBs and MSBs would be required to notify the Commission if they fail to make and keep current the required books and records on the same day that the failure arises. Broker-dealer SBSBs, broker-dealer MSBs, and stand-alone SBSBs would be required to notify the Commission of any material weakness within 24 hours of the discovery or notification. Finally, SBSBs would be required to notify the Commission if they fail to make a required deposit into their SB swap customer reserve account.

Jennifer S. Choi  
Senior Associate Counsel Securities Regulation

#### **endnotes**

[1] Recordkeeping and Reporting Requirements for Security-Based Swap Dealers, Major Security-Based Swap Participants, and Broker-Dealers; Capital Rule for Certain Security-Based Swap Dealers, Release No. 34-71958, available at <http://www.sec.gov/rules/proposed/2014/34-71958.pdf> (“Proposal”).

[2] Part 1 would apply to nonbank SBSBs and nonbank MSBs (i.e., broker-dealer SBSBs, broker-dealer MSBs, stand-alone SBSBs, and stand-alone MSBs).

[3] Part 2 would apply to bank SBSBs and bank MSBs.

[4] Part 3 would apply to an SBSD or MSBS that is dually registered as a futures commission merchant (“FCM”).

[5] Part 4 would apply to nonbank SBSBs and nonbank MSBs.

[6] Part 5 would apply to bank SBSBs and bank MSBs.

[7] Prudential regulators have established five capital categories that are used to describe a bank’s capital strength, which are based on capital measures under the bank capital standards and other factors. A bank is required to notify its appropriate prudential regulator of adjustments to the bank’s capital category.