

BROKER-DEALER

Statement on Status of the Consolidated Audit Trail

On August 27, the Securities and Exchange Commission's Division of Trading and Markets issued a public statement on the status of the consolidated audit trail (CAT) and the SROs' (defined below) currently expected timetable for compliance with their obligations under the revised Plan (defined below).

As discussed in a previous edition of *Corporate and Financial Weekly Digest*, the various national securities exchanges and the Financial Industry Regulatory Authority (the SROs) filed with the SEC a plan (Plan) to create, implement and maintain a CAT to capture information related to customers and order events for transactions in National Market System (NMS) securities and over-the-counter equity securities. Under the Plan, the first phase of reporting to the CAT was required to begin on November 15, 2017.

Just before the November 2017 deadline, the SROs submitted an exemption request letter to the SEC, requesting that the SEC issue exemptive relief to delay the first phase and other deadlines by a year or more. The SEC did not issue the relief requested by the SROs. To date, the SROs have not begun reporting required data.

The Division of Trading and Markets requested that the SROs create a detailed "Master Plan" that would, among other things, set forth a catalog of material steps necessary to effectively implement the CAT, a revised timeline with detailed, objective and achievable milestones, and clearly defined obligations

Pursuant to the Master Plan, the "first phase" reporting will commence on November 15, 2018 (compared to November 15, 2017 under the Plan); the "second phase" for large broker-dealer reporting will commence on November 15, 2019 (compared to November 15, 2018, under the Plan); and all phases of small broker-dealer reporting will be complete by November 15, 2022 (compared to November 15, 2019 under the Plan). However, not all data and functionality required by the Plan will be available on those dates. For example, only equities data—not options data—will be included in the large broker-dealer reporting that will commence on November 15, 2019.

The SEC also notes that the SROs' Master Plan affects the temporary exemption that the SEC issued from the third phase of Securities Exchange Act Rule 13h-1 (the large trader rule). This temporary exemption is scheduled to expire on November 15, and covers all large trader transactions beyond those currently phased-in.

In light of the delay in implementing the CAT, industry participants have raised the issue of whether a further extension of the temporary exemption from phase three of the large trader rule is necessary or appropriate. If you would like to inform the Division staff of your views regarding the large trader exemption, please communicate with the staff through the following email address: TradingandMarkets@sec.gov and insert "Large Trader Phase 3" in the subject line.

More information is available [here](#).

DERIVATIVES

See “CFTC Releases No-Action Position on PCAOB Requirement to Communicate Critical Audit Matters” and “CFTC Grants No-Action Relief Relating to Counting Toward the Swap Dealer Registration *De Minimis* Threshold” in the CFTC section.

CFTC

CFTC Releases No-Action Position on PCAOB Requirement to Communicate Critical Audit Matters

On August 29, the Commodity Futures Trading Commission's Division of Swap Dealer and Intermediary Oversight (Division) issued a no-action letter confirming that it will not recommend enforcement action against a futures commission merchant (FCM) if the accountant's audit opinion included in the FCM's annual financial report does not include “critical audit matters” (or the absence thereof) as required by the Public Company Accounting Oversight Board (PCAOB) standards. CFTC regulations generally require accountants engaged in audits of FCMs to register with the PCAOB and to conduct FCM audits in accordance with PCAOB standards. In 2017, the PCAOB adopted AS 3101, which requires an auditor registered with the PCAOB to communicate any critical audit matters in its audit report related to the financial statements of public companies. “Critical audit matters” include matters that are communicated or required to be communicated to the audit committee and: (1) relate to the accounts or disclosures that are material to the financial statements; and (2) involve especially challenging, subjective or complex auditor judgment.

Under its existing regulatory authority, the PCAOB explicitly excluded SEC-registered broker-dealers reporting under Securities Exchange Act Rule 17a-5 from the critical audit matters provisions of AS 3101. However, the PCAOB does not have regulatory authority with respect to CFTC registrants and did not address the applicability of critical audit matters requirements to the audits of FCMs. Consequently, absent relief from the CFTC or its staff, FCM audits must comply with the critical audit matters requirement.

In granting no-action relief, the Division noted that customer protection regulations already require FCMs to provide significant disclosures to customers, including relevant information about the financial condition, operation and audits of an FCM (similar to broker-dealer customer protection requirements). The Division also noted that the benefits of applying the critical audit matters requirements to FCM audits are minimal, considering the additional compliance costs.

CFTC Letter No. 18-21 is available [here](#).

CFTC Grants No-Action Relief Relating to Counting Toward the Swap Dealer Registration *De Minimis* Threshold

On August 28, the Commodity Futures Trading Commission's Division of Swap Dealer and Intermediary Oversight (Division) issued time-limited, no-action relief, permitting certain insured depository institutions (IDIs) from counting certain swaps toward the swap dealer *de minimis* threshold. Relief was requested after certain IDIs experienced a spike in the demand for interest rate swaps from existing loan clients seeking to hedge interest rate risk by entering into floating to fixed interest rate swaps that would otherwise cause the IDIs to exceed the swap dealer *de minimis* threshold.

Under CFTC regulations, a person is not deemed to be a swap dealer if the swap dealing activity of the person and any entity controlling, controlled by, or under common control with such person does not exceed the aggregate gross notional amount threshold, currently \$8 billion, over the preceding 12-month period. In calculating whether an IDI has exceeded the *de minimis* threshold, a person may exclude certain swaps entered into with a customer in connection with originating a loan with that customer (IDI Exclusion). Among other conditions, the IDI Exclusion requires that a swap must be entered into no later than 180 days after the date of execution of the applicable loan agreement or the transfer of principal to the customer (180-Day Requirement).

Relief from the 180-Day Requirement was requested to accommodate what is expected to be a temporary, heightened demand for swaps that would otherwise disqualify IDIs from the IDI Exclusion. The Division granted relief provided that the swaps in question meet the following conditions:

1. The swaps are with existing loan clients of the IDI;
2. Each such client is a small- or medium-sized commercial entity (meaning annual revenues are under \$750 million); and
3. The swaps would qualify for the IDI Exclusion, but for the 180-Day Requirement.

In addition, the aggregate notional amount of the swaps that are not counted toward the *de minimis* threshold satisfying the criteria above may not exceed \$1.5 billion at any time during the relief period. The relief period began on August 28, and expires on December 31.

CFTC Letter 18-20 is available [here](#).

Senate Confirms Two CFTC Nominations

On August 28, the US Senate confirmed the nominations of Dawn Stump and Dan Berkovitz as commissioners of the Commodity Futures Trading Commission. With the addition of two new commissioners, all five commissioner positions have now been filled. Commissioners Brian D. Quintenz and Rostin Behnam and Chairman J. Christopher Giancarlo released statements following the Senate confirmation, which are available [here](#).

EU DEVELOPMENTS

ECON Publishes Report on Regulatory and Supervisory Relationships Between the EU and Third Countries

On August 29, the European Parliament's Committee on Economic and Monetary Affairs (ECON) published its report, dated July 18, on relationships between the European Union (EU) and third countries concerning financial services and supervision.

The report includes a motion for a European Parliament resolution, within which the following recommendations are set out:

1. Third countries must keep the European Supervisory Authorities (ESAs) informed of any national regulatory developments through the EU's future equivalence framework, and the EU's equivalence decision should require good regulatory and supervisory cooperation, as well as exchange of information. Likewise, third countries would also be expected to maintain a close dialogue with the EU.
2. The European Commission (EC) should provide a clear framework for a transparent, coherent and consistent application of equivalence procedures that introduces an improved process for the determination, review, suspension or withdrawal of equivalence. Unlike the draft report that was published on April 4, the report does not call on the EC to adopt a legislative act for this purpose. The EC should also assess the benefits of introducing an application process for granting equivalence for third countries.
3. The relevant ESA should subject equivalence decisions to ongoing monitoring (instead of the three-yearly review that was proposed in the draft report), the outcome of which should be made public. Such monitoring should address the relevant legislation, enforcement practices and supervisory practices in the third country concerned.
4. The EC should review the effectiveness of the current equivalence regime and assess whether it contributes to achieving a level playing field between the EU and third-country financial institutions, while preserving the financial stability of the EU. The EC should publish its findings together with any proposals for improvement.
5. The EC should report annually to the European Parliament on all decisions on equivalence and explain the rationale behind those decisions.

6. The ESAs should have the capacity and powers to collect, collate and analyze data to enable them to monitor third-country supervisory and regulatory frameworks. The ESAs and national competent authorities should also cooperate closely in order to share best practices and ensure uniform implementation of regulatory cooperation and activities with third countries.

The report, unlike the draft report, does not call for a financial services chapter as part of any potential future trade agreement between the EU and United States.

The European Parliament will consider the report in its plenary session to be held from September 10 to September 13.

The report is available to view [here](#).

EBA Publishes Consultation Paper on Amendments to the CRR Supervisory Reporting ITS Relating to Securitizations

On August 28, the European Banking Authority (EBA) published a consultation paper on amendments to the Commission Implementing Regulation (Implementing Regulation) containing implementing technical standards on supervisory reporting (ITS), relating to the new securitizations framework, which came into force in January.

The ITS set out the common reporting framework relating to capital requirements, own funds and liquidity reporting by credit institutions and investment firms that are subject to the Capital Requirements Regulation (CRR). They aim to collect information on credit institutions' and investment firms' compliance with prudential requirements under the CRR and related technical standards.

The EBA is proposing amendments to the Implementing Regulation to integrate changes in the new securitizations framework, and to foster consistency between reporting and disclosure requirements. It is also proposing amendments to reflect national competent authorities' ability to monitor and assess firms' risk profiles, and to obtain a view on the risks posed to the financial sector.

The deadline for responses is November 27, The EBA expects to submit the final draft of the ITS to the European Commission in April or May 2019. It foresees the first reference date for the application of the ITS to be on March 31, 2020, with an implementation period of approximately one year.

The proposed revisions to Annexes 1 and II of the ITS are available [here](#).

The consultation paper is available [here](#).

For more information, contact:

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EU DEVELOPMENTS

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