

## COMMODITY FUTURES TRADING COMMISSION

### 17 CFR Part 3

RIN 3038-AE56

#### Chief Compliance Officer Duties and Annual Report Requirements for Futures Commission Merchants, Swap Dealers, and Major Swap Participants

**AGENCY:** Commodity Futures Trading Commission.

**ACTION:** Final rule.

**SUMMARY:** The Commodity Futures Trading Commission (“Commission” or “CFTC”) is amending its regulations regarding certain duties of chief compliance officers (“CCOs”) of swap dealers (“SDs”), major swap participants (“MSPs”), and futures commission merchants (“FCMs”) (collectively, “Registrants”); and certain requirements for preparing, certifying, and furnishing to the Commission an annual report containing an assessment of the Registrant’s compliance activities.

**DATES:** This rule is effective September 26, 2018.

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#### SUPPLEMENTARY INFORMATION:

### I. Background

#### A. Statutory and Regulatory Background

As amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”),<sup>1</sup> sections 4d(d) and 4s(k) of the Commodity Exchange Act (“CEA” or “Act”) require each Registrant to designate an individual to serve as its CCO.<sup>2</sup> Sections 4s(k)(2) and (3) set forth certain requirements and duties for CCOs of SDs and MSPs, including the requirement to prepare and sign an annual compliance report (“CCO Annual Report”).<sup>3</sup> CEA section 4d(d) requires CCOs of FCMs to “perform such duties and responsibilities” as are established by

Commission regulation or the rules of a registered futures association.<sup>4</sup> On November 19, 2010, the Commission proposed regulations implementing the CCO requirements,<sup>5</sup> and in April 2012, the Commission adopted the final CCO regulations (“CCO Rules Adopting Release”).<sup>6</sup> For purposes of this release, § 3.3<sup>7</sup> and the related definitions in § 3.1 of the Commission’s regulations are herein referred to as the “CCO Rules.”

#### B. The Proposal

On May 8, 2017, the Commission published for public comment a Notice of Proposed Rulemaking (“Proposal”)<sup>8</sup> to amend the CCO Rules. In particular, the Proposal addressed certain CCO duties and requirements for preparing and furnishing the CCO Annual Report. The Proposal sought to incorporate knowledge gained through Commission staff’s experience in administering the implementation of § 3.3 and to more closely harmonize certain provisions with corresponding Securities and Exchange Commission (“SEC”) rules for CCOs of security-based swap dealers and major security-based swap participants (collectively, “SEC Registrants”).<sup>9</sup>

To provide greater clarity regarding the CCO reporting line required by section 4s(k)(2)(A) of the Act and § 3.3(a)(1), the Commission proposed to define “senior officer” in § 3.1 as “the chief executive officer or other equivalent officer of a registrant.” With regard to CCO duties, the Proposal would include additional language in § 3.3(d)(1) to clarify that the CCO’s duty with respect to administering policies and procedures would be specific to the Registrant’s business as an SD, MSP, or FCM, as applicable.<sup>10</sup> The Proposal

would also modify the language in § 3.3(d)(2) to clarify that the CCO must take “reasonable steps” to resolve conflicts of interest, and to require in § 3.3(d)(3) that a CCO take reasonable steps to ensure compliance with the Act and Commission regulations by, among other things, “ensuring the registrant establishes, maintains, and reviews written policies and procedures reasonably designed to achieve compliance.” The Commission further proposed to amend § 3.3(d)(4) and (5) to remove the requirement in each provision that the CCO consult with the board of directors or senior officer in connection with establishing procedures for addressing noncompliance issues. The Proposal also would clarify that policies and procedures are to be “reasonably designed” to achieve their stated purpose, and would amend § 3.3(d)(4) to include remediating matters identified “through any means.”

Regarding the CCO Annual Report requirements, the Proposal would clarify § 3.3(e) by eliminating the requirement that a Registrant address “each” applicable CFTC regulatory requirement to which it is subject when assessing its written policies and procedures (“WPPs”). Additionally, the Commission proposed to clarify that the CCO Annual Report’s discussion of compliance resources be limited to a discussion of resources for the specific activities for which the Registrant is registered. Finally, the Proposal would amend § 3.3(f)(1) to add the Registrant’s audit committee (or equivalent body) as a required recipient of the CCO Annual Report in addition to the board of directors and the senior officer.

#### C. Harmonization With SEC Regulations

Using language identical to CEA section 4s(k), the Dodd-Frank Act amended the Securities Exchange Act of 1934 by adding section 15F(k) to establish CCO requirements for SEC Registrants.<sup>11</sup> In compliance with sections 712(a)(1)–(2) of the Dodd-Frank Act, the Commission and SEC staffs consulted and coordinated together, and with prudential regulators, in developing the respective CCO rules for purposes of regulatory consistency.<sup>12</sup>

The SEC initially proposed rule 15Fk-1 to implement CCO requirements and duties for SEC Registrants in July

is clarifying in the final rules that the CCO’s duties extend only to the activities of the registrant that are regulated by the Commission, namely swaps activities of SDs and MSPs and the derivatives activities included in the definition of FCM under section 1(a)(28) of the CEA.”)

<sup>11</sup> 15 U.S.C. 78o–10(k).

<sup>12</sup> Public Law 111–203, 124 Stat. 1376, 1641–1642 (codified at 15 U.S.C. 8302(a)(1)–(2)).

<sup>1</sup> See Dodd-Frank Act, Public Law 111–203, 124 Stat. 1376 (2010).

<sup>2</sup> 7 U.S.C. 6d(d) and 6s(k)(1).

<sup>3</sup> 7 U.S.C. 6s(k)(2) and (3).

<sup>4</sup> 7 U.S.C. 6d(d).

<sup>5</sup> See Designation of a Chief Compliance Officer; Required Compliance Policies; and Annual Report of a Futures Commission Merchant, Swap Dealer, or Major Swap Participant, 75 FR 70881 (proposed Nov. 19, 2010).

<sup>6</sup> 17 CFR 3.3(d)–(f). See Swap Dealer and Major Swap Participant Recordkeeping, Reporting, and Duties Rules, 77 FR 20128 (Apr. 3, 2012).

<sup>7</sup> 17 CFR 3.3 (2017). Commission regulations are found at 17 CFR chapter I, and may be accessed through the Commission’s website, [www.cftc.gov](http://www.cftc.gov).

<sup>8</sup> Chief Compliance Officer Duties and Annual Report Requirements for Futures Commission Merchants, Swap Dealers, and Major Swap Participants; Amendments, 82 FR 21330 (proposed May 8, 2017).

<sup>9</sup> See Business Conduct Standards for Security-Based Swap Dealers and Major Security-Based Swap Participants, 81 FR 29960 (May 13, 2016) (“SEC Adopting Release”).

<sup>10</sup> As noted in the Proposal, the change to referencing the Registrant’s business as an SD or MSP is not intended to affect the scope of the duties of the CCO. 82 FR at 21332 (Citing the CCO Rules Adopting Release, 77 FR 20158 (“[T]he Commission

2011.<sup>13</sup> In May 2013, after the CFTC adopted the CCO Rules, the SEC reopened the comment period for its outstanding Dodd-Frank Act Title VII rulemakings, including rule 15Fk-1.<sup>14</sup> SEC staff continued to consult with CFTC staff leading up to the adoption of rule 15Fk-1 in May 2016.<sup>15</sup>

While the CFTC regulates derivatives markets and the SEC regulates securities markets, many of the participants in these markets are the same. Similar activities in these markets are often regulated by each agency in similar ways under similar statutory mandates.<sup>16</sup> In this regard, the CFTC and SEC have taken steps through ongoing communication and coordination to harmonize similar regulations, including the regulations addressed in this release.

Several of the proposed amendments would further harmonize CFTC and SEC regulations. More specifically, the following provisions in the Proposal align the CFTC CCO regulations with the corresponding SEC CCO regulations:

- Including a definition of “senior officer” in § 3.1 that is identical to the SEC’s definition;
- Including additional language in § 3.3(d)(1) to clarify that the CCO’s duty with respect to administering policies and procedures would be specific to the Registrant’s business as an SD, MSP, or FCM, as applicable;
- Modifying the language in § 3.3(d)(2) to require reasonable steps be taken to resolve conflicts of interest;
- Requiring the CCO to identify noncompliance issues “through any means”;
- Removing the additional requirement in § 3.3(d)(4) and (5) that the CCO consult with the board of directors or senior officer in connection with establishing procedures for addressing noncompliance issues; and
- Replacing the requirement in § 3.3(e) that a Registrant address “each” applicable CFTC regulatory requirement to which it is subject when assessing its

<sup>13</sup> See Business Conduct Standards for Security-Based Swap Dealers and Major Security-Based Swap Participants, 76 FR 42396 (proposed Jul. 18, 2011).

<sup>14</sup> See Reopening of Comment Periods for Certain Rulemaking Releases and Policy Statement Applicable to Security-Based Swaps, 78 FR 30800 (May 23, 2013).

<sup>15</sup> 17 CFR 240.15Fk-1. See SEC Adopting Release, 81 FR 29960.

<sup>16</sup> For example, the provisions of the Dodd-Frank Act that provide for establishing regulations for swap dealers by the CFTC are nearly identical to most of the provisions of the Dodd-Frank Act that provide for establishing regulations for security-based swap dealers by the SEC. See Dodd-Frank Act, Public Law 111-203, 124 Stat. 1376, 1711-1712, 1793 (2010) (codified at 7 U.S.C. 6s and 15 U.S.C. 78o-10).

WPPs with a requirement to address the applicable regulations generally.

Furthermore, in the Proposal, the Commission solicited comments regarding potential additional rule changes that would further harmonize the CFTC and SEC regulations. After careful review of the comments received, the final rule includes the following additional harmonizing amendments:

- In § 3.3(d)(2), the CCO must take reasonable steps to resolve any “material” conflicts of interest;
- In § 3.3(d)(4), the CCO must “take reasonable steps to ensure the registrant” establishes, maintains, and reviews written policies and procedures for the remediation of noncompliance issues;
- In § 3.3(d)(5), the CCO must “take reasonable steps to ensure the registrant” establishes written procedures for the handling of noncompliance issues; and
- In § 3.3(f)(3), the CCO Annual Report certification includes language from the certifying individual that the CCO Annual Report is accurate and complete “in all material respects.”

## II. Summary of Comments

The Commission received eleven comment letters and Commission staff participated in one ex parte teleconference concerning the Proposal.<sup>17</sup> The majority of commenters generally supported the Commission’s efforts to clarify the role and duties of the CCO, reduce burdens associated with preparing the CCO Annual Report, and further harmonize the CCO Rules with parallel SEC rules. One commenter expressed general support for the proposed modifications and recognition of the Commission’s efforts as a meaningful step towards increasing regulatory certainty.<sup>18</sup> Another commenter expressed concern that a number of the proposals weaken the CCO regulatory regime (by, among other things, reducing CCO accountability).<sup>19</sup> Two comments exclusively sought clarity on the Proposal’s impact on the

<sup>17</sup> Comment letters were submitted by the following entities: Allen & Overy LLP; Automated Compliance Management, LLC (“ACM”); Better Markets; Chris Barnard; Futures Industry Association and Securities Industry and Financial Markets Association (“FIA/SIFMA”); International Swaps and Derivatives Association (ISDA); Japanese Bankers Association (“JBA”); National Futures Association (“NFA”); the Natural Gas Supply Association (“NGSA”); Paws Nutritional Org.; and TD Ameritrade Futures and Forex LLC (“TD Ameritrade”). All comment letters are available on the Commission’s website at <http://comments.cftc.gov/PublicComments/CommentList.aspx?id=1811>.

<sup>18</sup> See NGSA comment letter.

<sup>19</sup> See Better Markets comment letter.

continued ability of non-U.S. SDs to benefit from the Commission’s substituted compliance determinations that pertain to § 3.3.<sup>20</sup> Some commenters cautioned against complete harmonization with the SEC regarding the requirement to furnish the CCO Annual Report, but requested more complete alignment in other areas addressing the role and duties of the CCO.<sup>21</sup> As outlined below, several commenters suggested modifications to the rule text and requested further interpretive guidance regarding the role and duties of the CCO and CCO Annual Report content.<sup>22</sup> Additionally, several commenters suggested modifications to the rule text to add a materiality qualifier to the CCO Annual Report certification.<sup>23</sup> For the reasons provided below, the Commission accepted some of these recommendations in the amendments, as adopted, and accompanying guidance, and declined to accept certain other recommendations.

## III. Final Rule

### A. Regulation 3.1—Definitions

#### 1. Regulation 3.1(j)—“Senior Officer”

The Commission proposed to define “senior officer” in § 3.1 as “the chief executive officer or other equivalent officer of a registrant.” The Commission received four comments addressing the proposed definition.<sup>24</sup> Chris Barnard and Better Markets supported the proposed definition. FIA/SIFMA requested that the Commission address the variety of organizational structures present among Registrants and define “senior officer” to include “a more senior officer within the Registrant’s group-wide compliance, risk, legal or other control function who in turn reports to the holding company’s board of directors or CEO (or equivalent officer).”<sup>25</sup> FIA/SIFMA further requested that the Commission expand its interpretation of the phrase “other equivalent officer” to include the most senior officer of a Registrant with supervisory responsibility for all of the

<sup>20</sup> See Allen & Overy and JBA comment letters.

<sup>21</sup> See, e.g., FIA/SIFMA and ISDA comment letters.

<sup>22</sup> See, e.g., Better Markets, FIA/SIFMA, ISDA, NFA, and TD Ameritrade comment letters.

<sup>23</sup> See FIA/SIFMA, ISDA, and NFA comment letters.

<sup>24</sup> See Chris Barnard, Better Markets, ISDA, and FIA/SIFMA comment letters.

<sup>25</sup> See FIA/SIFMA comment letter. Similarly, while TD Ameritrade did not comment directly on the proposed definition, it requested that the Commission consider including a variety of senior roles at a Registrant for inclusion in the definition of “other equivalent officer” for purposes of allowing the CCO to report to someone other than the CEO.

Registrant's business as an FCM, SD, or MSP. ISDA expressed support for the Commission's proposed definition, but requested the Commission provide Registrants the ability to determine individually who would qualify as an "equivalent officer."

Upon consideration of the comments, the Commission is adopting the definition as proposed. This definition of "senior officer" clarifies the Commission's long-standing interpretation that compliance with the statutory requirement to have the CCO "report directly to the board or to the senior officer"<sup>26</sup> requires a CCO to have a *direct reporting line* to the board of directors or the highest executive officer in the legal entity that is the Registrant.<sup>27</sup>

As stated in the Proposal, the "chief executive officer" is typically the highest executive level, but the Commission is including in the definition the phrase "other equivalent officer" to address Registrants who may have a different title for the highest executive officer.<sup>28</sup> This approach is also consistent with the SEC's definition of "senior officer" in SEC rule 15Fk-1(e)(2), and is intended to ensure the CCO's independence from influence, interference, or retaliation.<sup>29</sup> The Commission is also declining to broaden its definition of "senior officer" or expand its interpretation of "other equivalent officer." The Commission notes that the definition of "senior officer," as adopted, does not preclude additional CCO reporting lines that Registrants may wish to implement for practical day-to-day oversight.<sup>30</sup>

In response to ISDA's comment, the Commission believes that the definition and guidance provide sufficient flexibility. Registrants should be able to ensure that regardless of a firm's chosen nomenclature, the CCO has a direct reporting line to the highest executive-level individual at the Registrant.

## 2. Other Definitions

In response to the Commission's request for comment regarding whether other definitions should be added to § 3.1, FIA/SIFMA requested that the

Commission define "material noncompliance issue" as it relates to the requirement in § 3.3(e)(5) to describe in the CCO Annual Report "any material noncompliance issues identified and the corresponding action taken." The Commission is declining to define "material noncompliance issue" at this time. Since the adoption of the CCO Rules, Registrants have defined and implemented their own materiality standards when categorizing non-compliance issues. Given the variation in size and nature of businesses among Registrants required to submit CCO Annual Reports, it is the Commission's view that materiality is dependent upon many factors that impact Registrants to varying degrees. While some factors ought to be considered by all Registrants, *e.g.*, whether the issue may involve a violation of the CEA or a Commission regulation, there is no "one size fits all" approach. Indeed, setting forth a standard of materiality could result in an overly prescriptive model for many Registrants. Based on experience in overseeing the implementation of § 3.3(e), Commission staff believes that Registrants have generally developed and applied adequate internal materiality standards for purposes of the CCO Annual Report.

### B. Regulation 3.3(d)—Chief Compliance Officer Duties

#### 1. Regulation 3.3(d)(1)—Duty To Administer Compliance Policies and Procedures

The Commission proposed to amend § 3.3(d)(1) to require that a CCO's duties include administering each of the registrant's policies and procedures relating to its business as a futures commission merchant, swap dealer, or major swap participant that are required to be established pursuant to the Act and Commission regulations.

ISDA and FIA/SIFMA generally supported the Commission's proposed changes<sup>31</sup> and recommended that the Commission further harmonize § 3.3(d)(1) with the SEC's CCO rules. Specifically, ISDA and FIA/SIFMA recommended that the Commission should clarify in guidance that the duty to administer policies and procedures means reviewing, evaluating, and advising the Registrant on its compliance policies and procedures.<sup>32</sup> Alternatively, ISDA proposed that the Commission strike the term "administering each" from § 3.3(d)(1), and replace it with "reviewing, evaluating, and advising the registrant

on the development, implementation, and monitoring" of the Registrant's compliance policies and procedures. ISDA asserted that the current proposed language creates an undue burden on CCOs who do not necessarily "administer" or execute each policy and/or procedure relating to an applicable CFTC rule. Rather, ISDA explained, various business units and control functions within a firm establish policies and procedures for their respective areas, with the ultimate supervisory authority residing with the CEO or other senior officer.

After considering the comments received, the Commission is adopting § 3.3(d)(1) as proposed. As the Commission has previously stated, and as discussed below, the role of the CCO, under the Dodd-Frank Act, goes beyond the customary and traditional advisory role of a CCO and requires more active engagement.<sup>33</sup> The Commission expects the CCO to be actively engaged in administering a firm's compliance policies and procedures, as described further below.

The language of § 3.3(d)(1), however, is not intended to diminish the role and direct involvement of other senior officers, supervisors and other employees with more direct knowledge, expertise, and responsibilities for various regulated activities within their business lines. Thus, while the CCO plays a central role in administering a firm's policies and procedures, other personnel may implement the procedures on a day-to-day basis when undertaking related activities in the normal course of business.

Furthermore, the Commission reiterates that the Registrant is ultimately responsible for the effective implementation of the policies and procedures.<sup>34</sup> In response to ISDA and FIA/SIFMA's request for clarification on the CCO's duty to administer policies and procedures, it is the Commission's view that a CCO may, in many circumstances, be able to fulfill his or her role through actively engaging in processes involving "reviewing, evaluating, and advising" on policies and procedures and compliance matters, while others in the organization are

<sup>26</sup> 7 U.S.C. 6s(k)(2)(A) (emphasis added).

<sup>27</sup> See CCO Rules Adopting Release, 77 FR at 20188. This concept was incorporated in § 3.3 and therefore applies to FCMs equally.

<sup>28</sup> Proposal, 82 FR at 21331. For example, some firms do not have a chief executive officer, but instead give the highest level executive the title of "president," "member," or "general partner."

<sup>29</sup> *Id.* See also CCO Rules Adopting Release, 77 FR at 20188.

<sup>30</sup> See CFTC Staff Advisory No. 16-62 (Jul. 25, 2016), available at <https://www.cftc.gov/idc/groups/public/%40rlrlettergeneral/documents/letter/16-62.pdf>.

<sup>31</sup> NFA also endorsed the proposed amendment to § 3.3(d)(1). See NFA comment letter.

<sup>32</sup> See SEC Adopting Release, 81 FR at 30057.

<sup>33</sup> See CCO Rules Adopting Release, 77 FR at 20162. ("In response to comments advocating a purely advisory role for the CCO, the Commission observes that the role of the CCO required under the CEA, as amended by the Dodd-Frank Act, goes beyond what has been represented by commenters as the customary and traditional role of a compliance officer.")

<sup>34</sup> See 75 FR 70881, 70883 (proposed Nov. 19, 2010). The CCO's duty to administer policies and procedures does not "otherwise contradict well-established tenets of law regarding the allocation of responsibility within a business association."

responsible for the daily implementation thereof. However, if, in the normal course, the CCO becomes aware (or reasonably should have been aware) of significant issues that are not being addressed in a reasonably satisfactory manner, the CCO is expected to take further action to address those issues. Importantly, for such circumstances, CEA section 4s(k)(2)(A) provides the CCO with a reporting line directly to the board or the senior officer. Accordingly, it may be appropriate for the CCO, depending on the facts and circumstances, to use that reporting line to elevate any such significant issues that have not been otherwise addressed satisfactorily. Through this active engagement and, if appropriate, utilizing the available escalation measures described above, the CCO may be able to demonstrate that he or she has fulfilled the role assigned to him or her under the regulation.

## 2. Regulation 3.3(d)(2)—Duty To Resolve Conflicts of Interest

Proposed § 3.3(d)(2) would require the CCO, in consultation with the board of directors or the senior officer, to take reasonable steps to resolve any conflicts of interest that may arise. ISDA and FIA/SIFMA supported the proposed revisions to § 3.3(d)(2) and provided additional recommendations. Both commenters recommended that the CCO's duty to resolve conflicts of interest should be limited to "material" conflicts of interest and should apply only to issues that arise in connection with the Registrant's business as an FCM, SD, or MSP. ISDA suggested that, consistent with the SEC's view, the Commission should explicitly state that the primary responsibility to resolve conflicts of interest falls on the Registrant and that the CCO's role would include identifying, advising, and escalating, as appropriate, to senior officers matters involving conflicts of interest. ISDA further suggested that the Commission replace "resolve" with "minimize" in the rule text. Similarly, FIA/SIFMA recommended that the Commission clarify that "resolution" involves either negation or mitigation of the conflict of interest.

Better Markets generally did not support the Commission's proposed changes to § 3.3(d)(2). Among other reasons, Better Markets is of the view that the proposed changes are not consistent with applicable statutory language to "resolve any conflicts" and will dilute the CCO's duty to address conflicts of interest.

Having considered these comments, the Commission is adopting § 3.3(d)(2)

as proposed but with further modifications to provide that CCOs have a duty to take reasonable steps to resolve "material" conflicts of interest "relating to the registrant's business as a futures commission merchant, swap dealer, or major swap participant." The additional language refines the Commission's view that CCOs cannot reasonably be expected to personally resolve every potential conflict of interest that may arise, and the Commission affirms that "routinely encountered conflicts could be resolved in the normal course of business . . ." consistent with the CCO's general administration of internal policies and procedures, which must include conflicts of interest policies.<sup>35</sup> Requiring the CCO to resolve every conflict of interest, including non-material conflicts, in consultation with the board of directors or the senior officer would potentially take too much of the CCO's and senior management's time away from other necessary activities when non-material conflicts can usually be resolved effectively by other staff in the normal course of business. The Commission believes that this is consistent with the underlying objective of this provision, which imposes a duty on CCOs to resolve matters under the Act and Commission regulations within the practical limits of their position at the Registrant. The Commission believes that the additional language does not dilute the CCO's duty to address conflicts of interest, and that the rule as amended fulfills the purposes of CEA section 4s(k).<sup>36</sup> Rather than spreading time and resources over many conflict issues—both material and non-material—the changes will allow the CCO to focus his or her time and resources on the material conflict issues, and more broadly, the other important compliance duties required by regulation. The Commission is also of the view that amending § 3.3(d)(2) to limit the scope of the CCO's responsibility to conflicts relating to the Registrant's business as an FCM, SD, or MSP clarifies that CCOs have a duty to resolve matters under the Act and Commission regulations, rather than any conflict that "may arise."

The Commission declines to implement comments suggesting that CCOs have a duty to simply minimize, rather than "resolve" conflicts of

<sup>35</sup> See Proposal, 82 FR at 21332. The addition of a materiality qualifier also further harmonizes § 3.3(d)(2) with the SEC's parallel CCO rule. See 17 CFR 240.15Fk-1(b)(3).

<sup>36</sup> See 77 FR at 21332 ("If strictly interpreted, the current rule text creates an undue burden on CCOs, likely taking them away from more important compliance activities.")

interest. CEA section 4s(k)(2)(C) explicitly requires conflict resolution.<sup>37</sup> While resolution can include the mitigation of conflicts to the point where they are no longer material, resolution also encompasses the elimination of conflicts if reasonably practicable.<sup>38</sup>

In response to ISDA's request that the Commission state that a CCO's role in resolving conflicts would involve identifying, advising on, and escalating to management conflicts of interest, the Commission is declining to incorporate that language into the regulatory text. However, the Commission believes that such an approach provides a reasonable framework for CCOs to use in fulfilling their duty to take reasonable steps to resolve material conflicts of interest. As the Commission has previously acknowledged, active engagement "may involve actions other than making the final decision."<sup>39</sup>

Should CCOs choose to incorporate the "identify, advise and escalate" framework into their conflict resolution procedures, however, a passive implementation of that framework should not be viewed as fulfilling the CCO's duties for conflict resolution. The requirement to "take reasonable steps" requires an active role in the conflict resolution process, including, for example: (1) Direct involvement of the CCO in developing and implementing active processes for conflict identification, evaluation, and resolution; (2) advising on the effectiveness of alternatives to mitigate or eliminate conflicts; and (3) escalating conflict issues if the conflicts are not otherwise resolved or mitigated as required by § 3.3(d)(2), including through the CCO's direct reporting line to the board of directors or the senior officer if necessary or appropriate.

The Commission believes that the determination of what is a "material" conflict for a particular Registrant should be assessed based on the facts and circumstances relevant to that Registrant and the conflict. Although the Commission notes that there are some conflicts that are typically treated as material,<sup>40</sup> the Commission declines

<sup>37</sup> See 7 U.S.C. 6s(k)(2)(C).

<sup>38</sup> See CCO Rules Adopting Release, 77 FR at 20161.

<sup>39</sup> *Id.*

<sup>40</sup> For example, similar to the SEC's approach, conflicts between the business interests of a Registrant and its regulatory requirements, and conflicts between or with associated persons of a Registrant are often material. See SEC Adopting Release, 81 FR 29960 at 30056-30057 ("Such conflicts of interest could include conflicts between the commercial interests of an SBS Entity and its statutory and regulatory responsibilities, and

at this time to define materiality in this context to avoid creating an unintentionally prescriptive model. The Commission expects each Registrant to develop its own appropriate standard or procedure for determining if a conflict is “material” for purposes of the rule.

### 3. Regulation 3.3(d)(3)—Duty To Ensure Compliance

The Proposal would make a wording change to § 3.3(d)(3) to simplify the text<sup>41</sup> and to add that a CCO’s duty in § 3.3(d)(3) to ensure compliance with the Act and the Commission’s regulations includes “ensuring the registrant establishes, maintains, and reviews WPPs reasonably designed to achieve compliance.”

ISDA and FIA/SIFMA recommended that the Commission further harmonize paragraph (d)(3) with the SEC’s corresponding rule by removing the existing general duty for the CCO to take reasonable steps to ensure compliance and only require the CCO to ensure that the Registrant establishes, maintains, and reviews policies and procedures as the CCO’s duty.<sup>42</sup> ISDA and FIA/SIFMA also asserted that the change would address uncertainty regarding the breadth of a CCO’s supervisory authority and concerns that ensuring compliance is an impracticable requirement for CCOs.

TD Ameritrade commented that the Commission should align paragraph (d)(3) with FINRA Rule 3130 by clarifying that the CCO is required to “have processes in place” for the Registrant to establish, maintain, and review WPPs reasonably designed to achieve compliance. TD Ameritrade contended that the proposed language in paragraph (d)(3), which requires CCOs to ensure compliance, rather than simply have processes in place, is cumbersome and perhaps places a higher burden on CCOs than intended by the Commission.

Better Markets commented that the proposed amendment to paragraph (d)(3) could be viewed as defining the full scope of the CCO’s duty to ensure compliance, rather than merely clarifying the extent of the duty. Better Markets noted that the duty to ensure compliance is broad and cannot be

conflicts between, among, or with associated persons of the SBS Entity.”).

<sup>41</sup> The Proposal would change the words “. . . relating to the swap dealer’s or major swap participant’s activities, or to the future commission merchant’s business as a futures commission merchant” to “. . . relating to the registrant’s business as a futures commission merchant, swap dealer or major swap participant.”

<sup>42</sup> See FIA/SIFMA and ISDA comment letters (emphasis added). See also 17 CFR 240.15Fk–1(b)(2).

equated with a CCO’s obligation to administer policies and procedures. To eliminate uncertainty, Better Markets recommended further clarifying that the additional language is “without limitation.”<sup>43</sup>

Having considered the totality of the responses received, the Commission believes that the proposed amendment to § 3.3(d)(3) adding that the duty includes “ensuring the registrant establishes, maintains, and reviews WPPs reasonably designed to achieve compliance” creates ambiguity, rather than clarity, with respect to the scope of a CCO’s duty to ensure compliance. Therefore, the Commission is declining to adopt that proposed amendment to § 3.3(d)(3).<sup>44</sup> A CCO’s duty in § 3.3(d)(3) to ensure compliance with the Act and Commission regulations therefore remains the same as adopted in the CCO Rules Adopting Release.

Current § 3.3(d)(3) implements CEA section 4s(k)(2)(E). CEA section 4s(k)(2)(E) requires that the CCO shall ensure compliance with the Act (including regulations) relating to swaps, including each rule prescribed by the Commission under that section. Thus, the Commission believes § 3.3(d)(3) requires more than, as suggested by some commenters, simply taking reasonable steps to ensure the Registrant establishes, maintains, and reviews written compliance policies and procedures.<sup>45</sup> The Commission, however, acknowledges commenters’ concerns regarding the uncertainty as to the breadth of a CCO’s responsibility and the practicality of broad expectations for the CCO in this regard given the wide variety of swap dealing and other activities undertaken by different Registrants. When finalizing § 3.3(d)(3), the Commission recognized that requiring a CCO to “ensure compliance” could be an impracticable standard and limited the CCO’s duty to “taking reasonable steps to ensure compliance.”<sup>46</sup> At the time, however, the Commission did not provide guidance on what “taking reasonable steps to ensure compliance” means. Accordingly, the Commission is taking this opportunity, with the benefit of several years of experience implementing the CCO Rules, to provide further guidance as to the breadth of the

<sup>43</sup> Better Markets comment letter.

<sup>44</sup> The proposed non-substantive change that simplifies the wording of § 3.3(d)(3) is being adopted for the reasons stated in the Proposal.

<sup>45</sup> See 7 U.S.C. 6s(k)(2)(E) (requiring the CCO to ensure compliance with the Act (including regulations) relating to swaps, including each rule prescribed by the Commission under that section).

<sup>46</sup> See CCO Rules Adopting Release, 77 FR at 20162.

CCO obligations under § 3.3(d)(3) and the practical expectations for fulfilling those obligations.

As stated by the Commission previously, the CCO’s duty to take reasonable steps to ensure compliance includes active engagement in the day-to-day implementation of compliance policies and procedures.<sup>47</sup> This engagement would likely include a reasonable level of involvement in compliance monitoring, identifying non-compliance or potential non-compliance events, advising on the mitigation and correction of compliance activities, and, where necessary, escalating significant matters that require senior management attention.<sup>48</sup> Whether the CCO’s activities constitute “reasonable steps” depends on the facts and circumstances of the Registrant’s related business activities, such as the size of the business, the diversity and complexity of the swaps or FCM activities, and the overlap with other compliance activities in the firm (e.g., where swap dealing activities may be contained within business lines that are subject to additional regulation outside the CEA).

In taking reasonable steps to ensure compliance, the Commission believes that a CCO cannot reasonably be expected to have sole and complete responsibility for ensuring compliance with the Act and the relevant regulations.<sup>49</sup> As such, § 3.3(d)(3) does not require the CCO to guarantee compliance or be granted final supervisory authority.<sup>50</sup> The regulation does not diminish the role and direct involvement of other senior officers, supervisors, and employees with more direct knowledge, expertise, and responsibilities for the regulated business activities to effect compliance. As such, the Commission is of the view that a CCO may reasonably rely on these personnel to implement many of the policies and procedures needed to ensure compliance as part of their regular business activities (in this regard, such personnel are sometimes referred to as the “first line” of compliance).<sup>51</sup> The Commission also

<sup>47</sup> See supra at note 33.

<sup>48</sup> For example, escalation could be to the board or the senior officer to whom the CCO reports either through the CCO Annual Report, annual or more frequent meetings, or other mechanisms.

<sup>49</sup> See 75 FR at 70883 (“The chief compliance officer can only ensure the registrant’s compliance to the full capacity of an individual person . . .”).

<sup>50</sup> See CCO Rules Adopting Release, 77 FR at 20162 (“[T]he Commission does not believe . . . that the CCO’s duties under the CEA or § 3.3 requires that the CCO be granted ultimate supervisory authority by a registrant.”).

<sup>51</sup> For example, in working with other personnel at the Registrant, it would be reasonable to expect

notes that, pursuant to § 3.3(a)(1), the CCO has a direct reporting line to the board or the senior officer of the Registrant. To the extent the CCO determines that he or she cannot fulfill the duty established in § 3.3(d)(3) because of the actions or inaction of others, a lack of resources, or otherwise, the CCO has an avenue for escalating these issues to the highest level of management within the Registrant. In doing so, the CCO may be able to demonstrate that he or she has taken reasonable steps to fulfill the duty created in § 3.3(d)(3).

#### 4. Regulation 3.3(d)(4) and (5)—Duty To Remediate Noncompliance Issues

The Commission proposed to amend § 3.3(d)(4) by adding language that the duty to remediate noncompliance issues identified by the CCO encompasses maintaining and reviewing, in addition to establishing, written policies and procedures. The Commission also proposed to amend § 3.3(d)(4) and (5) by removing the requirement that the CCO consult with the board of directors or senior officer in establishing: (1) Policies and procedures for the remediation of noncompliance issues identified by the CCO; and (2) procedures for the handling, management response, remediation, retesting, and closing of noncompliance issues. The Proposal would also clarify that the policies and procedures should be “reasonably designed” to remediate noncompliance issues. Lastly, the Commission proposed to amend paragraph (d)(4) to include the remediation of matters identified “through any means” by the CCO, including the specific discovery methods already listed in § 3.3(d)(4). FIA/SIFMA generally supported the Commission’s proposed amendments to paragraphs (d)(4) and (5), and requested that the Commission further add to paragraphs (d)(4) and (5) that the CCO’s duty is to take “reasonable steps to ensure that the registrant” establishes the required policies and procedures for the remediation of noncompliance issues, rather than to be directly responsible for establishing the policies and procedures. FIA/SIFMA noted that this change, consistent with the SEC’s CCO rules, reflects the fact that it is the responsibility of the Registrant, not the

that a CCO would participate in (though not necessarily have sole or principal responsibility for implementing) the development and implementation of compliance training, monitoring and spot checking of first line compliance activities, the identification of possible compliance weaknesses, and the escalation to supervisors and senior management of the remediation or mitigation of weaknesses identified, as appropriate.

CCO in his or her personal capacity, to establish the specified policies and procedures.

Better Markets disagreed with the Commission’s proposed changes. Better Markets contended that the removal of the board of directors and senior officer consultation requirement could marginalize the board of directors’ role and send the message that the board of directors needs to be only occasionally involved in the remediation of noncompliance issues. Better Markets further asserted that the proposed change that policies and procedures be “reasonably designed” makes it easier for Registrants to meet their legal obligations without actually realizing the underlying regulatory goal of remediating noncompliance issues.

With respect to the specific noncompliance discovery methods listed in paragraph (d)(4), ISDA recommended that the Commission provide legal certainty to Registrants by clarifying that the term “complaint that can be validated” means “a written complaint that can be supported upon a reasonable investigation.”<sup>52</sup> ISDA noted that this clarification would further harmonize the Commission’s CCO Rules with the SEC’s, and would provide legal certainty with respect to which kinds of noncompliance issues need to be escalated to the CCO.

In light of the comments received, the Commission is adopting proposed paragraphs (d)(4) and (5) with additional modifications to clarify the Commission’s position that the CCO’s duty with respect to establishing the Registrant’s noncompliance remediation policies and procedures is to take reasonable steps to ensure that the registrant fulfills that responsibility. Accordingly, § 3.3(d)(4) and (5), as adopted, require a CCO to take “reasonable steps to ensure the registrant” establishes, maintains and reviews the applicable policies and procedures. With respect to the other proposed amendments to paragraphs (d)(4) and (5), the Commission is adopting those amendments for the reasons discussed in the Proposal.

In response to the concern raised by Better Markets that removing the consultation clause will diminish the board of directors and senior officer role, the Commission believes that there are two reasons to maintain the proposed changes to § 3.3(d)(4) and (5). As discussed in the Proposal, the CCO should manage and remediate noncompliance issues in consultation, as appropriate, with personnel that are experts in these matters, including, if

appropriate, senior management and the board of directors. Requiring further consultation with the board of directors or the senior officer on these procedures in the ordinary course would be an unnecessary burden on the Registrants. Furthermore, the Commission notes that, under § 3.3(a)(1), the CCO must report to the board of directors or the senior officer. Accordingly, to the extent the CCO is of the view that the policies and procedures being established do not meet the requirements of the Commission’s regulations and is unable to effect the necessary changes through other means, it would be appropriate for the CCO, as a reasonable step for ensuring that the appropriate policies and procedures are established, to elevate the issue to the board of directors or the senior officer to whom the CCO reports. Thus, an appropriate avenue for consultation with the board of directors or the senior officer is already part of the regulatory requirements in the CCO Rules.

With respect to ISDA’s recommendation that the Commission clarify the “complaint that can be validated” standard, the Commission declines to clarify the standard in the manner requested. The Commission believes that noncompliance should be a focus for CCOs, and accordingly, all noncompliance complaints, whether written or verbal, should be investigated using reasonable means. The Commission further notes that the CCO may identify noncompliance issues “through any means” and “a complaint that can be validated” is one of many ways in which a CCO may identify such issues.

#### C. Regulation 3.3(e)—CCO Annual Report

Below is a subsection-by-subsection review of the comments received on the proposed changes to the CCO Annual Report requirements and a description of the changes being adopted.<sup>53</sup> On December 22, 2014, CFTC staff issued Advisory No. 14–153 providing guidance to Registrants on the form and content requirements of the CCO Annual Reports (“CCO Annual Report Advisory”). In their comment letter, FIA/SIFMA requested that the Commission address the effect of the rule amendments on the guidance in the CCO Annual Report Advisory.

The Commission believes that providing updated guidance in concert

<sup>53</sup> In connection with the proposed amendments, the Proposal also would renumber the paragraphs within § 3.3(e) and make other non-substantive changes related to the renumbering. Those changes are being adopted for the reasons stated in the Proposal.

<sup>52</sup> ISDA comment letter.

with adopting the amendments to § 3.3(e) will help to increase the final rule's efficiency and clarity.

Accordingly, the Commission is providing guidance regarding the CCO Annual Report in new Appendix C to Part 3, "Guidance on the Application of Rule 3.3(e), Chief Compliance Officer Annual Report Form and Content." The CCO Annual Report Advisory is hereby superseded by this final release including the new Appendix C to Part 3. The Commission or its staff may issue updated guidance regarding the CCO Annual Report in the future based on experience gained as Registrants implement the amended content requirements.

#### 1. Regulation 3.3(e)(1)—Description of the Registrant's WPPs

Section 3.3(e)(1) requires a CCO to describe the Registrant's WPPs, including its code of ethics and conflicts of interest ("COI") policies. Proposed § 3.3(e)(1) sought to clarify that only the WPPs that relate to a Registrant's business as an FCM, SD, or MSP must be described in the CCO Annual Report by adding text referring to the policies and procedures described in § 3.3(d). The Commission did not receive any comments specific to proposed § 3.3(e)(1),<sup>54</sup> and is adopting amended § 3.3(e)(1) as proposed.<sup>55</sup>

#### 2. Regulation 3.3(e)(2)—Assessment of the Effectiveness of the Policies and Procedures

Proposed § 3.3(e)(2) would eliminate the express mandate to identify and assess the effectiveness of each WPP for each regulatory requirement under the CEA and Commission regulations in the CCO Annual Report. The Commission received six comments regarding this proposed amendment. FIA/SIFMA, ISDA, NFA, and TD Ameritrade generally supported the change. Specifically, ISDA noted that the proposed revisions "would strike a proper balance between providing the Commission with meaningful analyses of firms' compliance programs and conserving the time and resources of both the Commission and firms."<sup>56</sup> Similarly, NFA stated, "NFA believes it will improve the quality of the report by allowing firms to focus on providing

meaningful summaries of their WPPs, together with a detailed discussion of the annual assessment and recommended improvements."<sup>57</sup>

Better Markets opposed the proposed amendment and expressed its belief that the "detailed assessment of the policies and procedures, relative to each specific regulatory requirement, is a valuable exercise that brings rigor to the process."<sup>58</sup> ACM explained that Registrants, using ACM's product, often obtain sub-certifications from subject matter experts within the firm for each applicable requirement. ACM sought clarification regarding whether the proposed amendment is intended to eliminate the requirement-by-requirement review.

The Commission has considered the comments and is adopting amended § 3.3(e)(2) as proposed. As adopted, the rule requires the CCO Annual Report to contain, among other things, a description of the CCO's assessment of the effectiveness of the Registrant's WPPs relating to its business as an FCM, SD, or MSP. In response to Better Markets and ACM, the Commission affirms that the rule, as amended, does not require the CCO Annual Report to contain an assessment of the WPPs' effectiveness with respect to *each* applicable requirement under the Act and regulations. However, the CCO must still conduct an underlying assessment of the policies and procedures to meet the requirements of the rule. The Commission affirms that Registrants may still rely on the use of sub-certifications or any other methodology they have previously employed to conduct the assessment of their compliance programs pursuant to § 3.3(d) and (e).

In further response to Better Markets' concern that removing the requirement-by-requirement assessment from the CCO Annual Report would weaken the self-assessment process, the Commission notes that the final rule does not remove a CCO's duty to undertake the review. The Commission believes that a robust and meaningful self-assessment process is maintained through the affirmative CCO duties to ensure review of the WPPs and to describe the CCO's assessment in the CCO Annual Report. Furthermore, as described in the Proposal, the Commission believes that reducing the burden associated with preparing the CCO Annual Report will permit CCOs and Registrants to both improve their compliance assessment processes and

allocate more time and resources to more critical areas within the firm.

#### 3. Regulation 3.3(e)(4)—Resources Set Aside for Compliance

Proposed § 3.3(e)(4) would clarify that the discussion of resources only need address those resources set aside for compliance activities that relate to the Registrant's business as an FCM, SD, or MSP. The Commission received comments from FIA/SIFMA, NFA, and ISDA generally supporting the proposed amendment. ISDA suggested that the Commission rescind related guidance in the CCO Annual Report Advisory regarding quantification of resources and allow Registrants to provide a narrative assessment of the sufficiency of compliance resources.<sup>59</sup> Similarly, FIA/SIFMA requested that the Commission state that Rule 3.3(e)(4) does not require specific numerical estimates.<sup>60</sup>

The Commission is adopting amended § 3.3(e)(4) as proposed. Regarding the description of compliance resources, the Commission previously addressed the issues raised by ISDA, FIA, and SIFMA in the CCO Rules Adopting Release. At the outset, the Commission has recognized that a primary purpose of the CCO Annual Report is to provide "an efficient means to focus the registrant's board and senior management on areas requiring additional compliance resources."<sup>61</sup> A detailed discussion of the current state of compliance resources, including as appropriate, quantitative information, forms an integral part of a CCO Annual Report that, as the Commission stated, "will help FCMs, SDs, MSPs and the Commission to assess whether the registrant has mechanisms in place to address adequately compliance problems that could lead to a failure of the registrant."<sup>62</sup> In requiring a description of the compliance resources in the CCO Annual Report, but not prescribing the description's form or manner (which is left to the Registrant's reasonable discretion) the Commission is balancing the need for context and critical information, and the potential burdens on the CCO in performing the underlying resources identification and analysis.<sup>63</sup>

The description of resources required by § 3.3(e)(4) is intended to inform the Registrant and the Commission as to the sufficiency of resources dedicated to

<sup>54</sup> Three commenters expressed general support of the proposed amendments to § 3.3(e). See TD Ameritrade, FIA/SIFMA, and ISDA comment letters.

<sup>55</sup> The Commission notes that § 3.3(e)(1) retains the statutory requirement in CEA section 4s(k)(3)(A)(ii), 7 U.S.C. 6s(k)(3)(A)(ii), to describe the Registrant's Conflict of Interest and Code of Ethics policies (if the Registrant had previously adopted a Code of Ethics).

<sup>56</sup> See ISDA comment letter.

<sup>57</sup> See NFA comment letter.

<sup>58</sup> See Better Markets comment letter.

<sup>59</sup> See ISDA comment letter.

<sup>60</sup> See FIA/SIFMA comment letter.

<sup>61</sup> See CCO Rules Adopting Release, 77 FR at 20190.

<sup>62</sup> *Id.* at 20193.

<sup>63</sup> *Id.* at 20164.

compliance. Moreover, by requiring inclusion in the CCO Annual Report, the Commission recognizes that the usefulness of this information may lie in the trends and impacts of isolated events that can be observed over time regarding staffing levels, financial resources devoted to compliance, or the addition or subtraction of operational or technological resources. Some of the categories of resources CCOs are required to describe under § 3.3(e)(4) are, by their nature, quantitative (*e.g.*, number of compliance personnel and budgetary information). However, the Commission also recognizes that, depending on a Registrant's structure and the nature of its business, a quantitative description may include approximations and estimates. It is the Commission's view that, in complying with § 3.3(e)(4), each Registrant should focus on whether its CCO Annual Report is effectively providing its senior leadership and the Commission with the ability to reasonably assess the state of the Registrant's compliance resources, irrespective of how it expresses the quantitative information.

#### *D. Regulation 3.3(f)—Furnishing the CCO Annual Report and Related Matters*

In view of the comments received on proposed § 3.3(f) and related matters, the Commission is making a number of changes described below. As a general matter, to provide the reader greater clarity, the Commission is adding descriptive paragraph headings to § 3.3(f)(1) through (6) for the final rule.

##### 1. Regulation 3.3(f)(1)—Furnishing the CCO Annual Report

Proposed § 3.3(f)(1) would harmonize the requirements under the SEC and CFTC CCO Rules to require that the CCO Annual Report be furnished to all members of the board of directors, senior officer, and audit committee (or equivalent body) prior to being furnished to the Commission.

The Commission received three comments addressing the proposed amendment. Better Markets supported the proposed amendment as a means to strengthen the CCO framework. ISDA and FIA/SIFMA opposed the amendment and asserted that it is burdensome and unnecessary in light of the variability among Registrants. Specifically, ISDA and FIA/SIFMA commented that the proposed amendment would add burdens and costs given that the audit committees and boards of directors do not necessarily meet prior to the deadline to file the CCO Annual Report with the

Commission.<sup>64</sup> FIA/SIFMA also contended that harmonization with the SEC is not appropriate for this rule because there is greater variety of corporate forms and organizational structures among FCMs, SDs, and MSPs than SEC-regulated entities and the change may raise questions for those Registrants that do not have a board of directors or audit committee. Additionally, FIA/SIFMA asserted the board of directors of an SD that is part of a large, diversified commercial bank may already have full meeting agendas that do not warrant the addition of another board obligation. Alternatively, ISDA and FIA/SIFMA commented that if the Commission decided to adopt the proposed amendment, it should make appropriate modifications to accommodate existing board and audit committee meeting schedules. FIA/SIFMA also sought further clarification that the rule would not require a Registrant to establish a board of directors or audit committee, and that it could be satisfied through submission to certain other equivalent personnel.

After considering commenters' concerns, the Commission has determined to retain the current approach in § 3.3(f)(1) to require the CCO to provide the annual report to the board of directors or the senior officer prior to furnishing it to the Commission.<sup>65</sup> The Commission, however, is also adopting a modified version of proposed § 3.3(f)(1) with respect to furnishing the CCO Annual Report to the audit committee (or equivalent body). In response to comments, § 3.3(f)(1)(ii), as adopted, requires that the CCO Annual Report must be furnished to the audit committee (or equivalent body), if the Registrant has such a committee. In addition, if the Registrant has an audit committee (or equivalent body), then the CCO Annual Report must be furnished to that committee not later than its next scheduled meeting after the date on which the CCO Annual Report is furnished to the Commission, but in no event more than 90 days after the Registrant's CCO Annual Report is furnished to the Commission. The Commission is adding the 90 day time frame to ensure that the audit committee receives the report in a timely manner in furtherance of this provision, but without causing unnecessary disruption to its operation.

<sup>64</sup> See ISDA and FIA/SIFMA comment letters.

<sup>65</sup> A conforming change was made to § 3.3(f)(1)(iii) regarding making and maintaining a record of furnishing the report to the board of directors or the senior officer, and the audit committee.

The Commission believes that a flexible approach to the timing of furnishing the CCO Annual Report to the audit committee (or equivalent body) addresses commenters' concerns about meeting schedules and the CCO Annual Report submission deadline and better serves the underlying purpose of furnishing the report to the appropriate representatives of senior management at a time that allows for appropriate review by them. The Commission further believes that although the rule as adopted is not identical to the SEC's approach, the two approaches both preserve the goal of ensuring that management with overall responsibility for governance and internal controls is informed of the Registrant's state of compliance in a timely manner while recognizing the inherent differences between CFTC and SEC Registrants. The SEC's CCO rules apply to security-based swap dealers and major security-based swap participants, which are likely to consist of a smaller number of large financial entities or affiliates thereof, most of which are likely required by regulation to have audit committees.<sup>66</sup> By contrast, the CFTC's CCO Rules apply to SDs that range from large financial enterprises to regional banks to commodity dealers to limited purpose affiliates, as well as FCMs. In light of this greater variety of firms subject to the CFTC CCO Rules, the Commission believes a more flexible approach is appropriate.

Similarly, in response to FIA/SIFMA's comment that some Registrants may not have a board of directors or audit committee, the Commission acknowledges that some types of entities that are Registrants are not required to have such bodies, particularly audit committees, and therefore may not have established such a body. The Commission affirms that the rule was not intended to require Registrants to establish either type of body. Accordingly, the final rule text provides that furnishment to the audit committee or equivalent body is required only if such a committee or body has been established. If not, compliance with § 3.3(f)(1) may be met by furnishing the CCO Annual Report to the senior officer or board members only, as applicable.

##### 2. Regulation 3.3(f)(3)—Certification

In response to the Commission's request for comment on additional changes to further harmonize with the

<sup>66</sup> See SEC Adopting Release, 81 FR at 30105 (estimating that approximately 55 entities might register as security-based swap dealers or major security-based swap participants).



SEC regulations that correspond to § 3.3(f), the Commission received four comments regarding the CCO Annual Report certification language in § 3.3(f)(3). Citing the Commission's stated goal of harmonizing § 3.3 with SEC rule 15Fk-1(c)(2)(ii)(D) and concerns regarding potential excess CCO liability, NFA, FIA/SIFMA, and ISDA urged the Commission to include a materiality qualifier. FIA/SIFMA and ISDA recommended that the phrase "in all material respects" be added. TD Ameritrade requested that the Commission assess whether the "under the penalty of law" standard is the correct standard for CCOs.

The Commission is adopting § 3.3(f) as proposed with one change. The Commission is adding qualifying language, "in all material respects" to the requirement to certify that the information contained in the CCO Annual Report is accurate and complete. Consistent with the SEC's approach, this modification provides a reasonable standard and additional clarity regarding the obligations and potential liability of the certifying official. When the Commission adopted the CCO Rules in 2012, it was of the view that limiting the certification language with the qualification "to the best of his or her knowledge and reasonable belief" would address concerns of overbroad liability.<sup>67</sup> The rule, the Commission reasoned, "would not impose liability for compliance matters that are beyond the certifying officer's knowledge and reasonable belief at the time of the certification."<sup>68</sup> This language, however, as noted by FIA/SIFMA, ISDA, and TD Ameritrade, may not completely address concerns regarding immaterial inaccuracies or omissions in the CCO Annual Report, notwithstanding the certifying official's good faith efforts to exercise appropriate due diligence.

As noted in the CCO Rules Adopting Release, the Commission appreciates that, for many Registrants, the breadth and complexity of the information contained in the CCO Annual Report inherently requires reliance on many individuals to gather the information for, and prepare, the report.<sup>69</sup> The Commission understands that immaterial inaccuracies or omissions rarely undermine the compliance information contained in the CCO Annual Report. Accordingly, it is reasonable and appropriate to expect that the CCO or chief executive officer would, "to the best of his or her

knowledge and reasonable belief" certify that "the information in the annual report is accurate and complete in all material respects" (emphasis added).<sup>70</sup>

### 3. Regulation 3.3(f)(6)—Incorporation by Reference and Treatment of Affiliated Registrants

FIA/SIFMA commented that, because affiliated SDs often share a common SD compliance program, much of the information in the CCO Annual Reports is the same. FIA/SIFMA therefore requested that the Commission permit flexibility in how reports from affiliated registrants address common matters.

The Commission believes that, as a procedural matter within the scope of this rulemaking, it is appropriate to provide the requested flexibility. Permitting the consolidation of all relevant information concerning Registrants that control, are controlled by, or are under common control with, other Registrants ("Affiliated Registrants") into one cohesive report could lead to greater efficiency for those Registrants and improved regulatory oversight. In addition, the request is consistent with provisions in § 3.3(f)(6) permitting individual Registrants and Registrants that are registered in more than one capacity, e.g., as an SD and FCM ("Dual Registrants"), to incorporate by reference sections of a CCO Annual Report furnished to the Commission within the current or immediately preceding reporting period. Accordingly, the Commission is amending § 3.3(f)(6) to permit Affiliated Registrants to incorporate within their CCO Annual Reports information shared across related Registrants.

More broadly, the Commission believes that the annual compliance reporting requirement should not be subject to restrictive formatting requirements that do not serve the purpose of the reports. To the extent that the same information can be presented once for multiple reporting requirements (e.g., for a Dual Registrant or Affiliated Registrants) thereby creating efficiencies without undermining the purpose and utility of the CCO Annual Report, the Commission believes it is appropriate to permit the practice. In view of the foregoing, the Commission is reorganizing § 3.3(f)(6) into three subparagraphs to more clearly set forth the different scenarios in which

Affiliated Registrants or Dual Registrants can present the same information used in multiple reports or file one combined report addressing multiple reporting requirements.

New subparagraph (i) incorporates without modification the current language in § 3.3(f)(6). Subparagraph (i) permits an individual Registrant to incorporate by reference sections in a CCO Annual Report that it furnished to the Commission within the current or immediately preceding reporting period.

Like § 3.3(f)(6) as originally adopted, new subparagraph (ii) permits Dual Registrants to cross-reference sections in CCO Annual Reports submitted on behalf of either of its registrations within the current or immediately preceding reporting period. To address ambiguity regarding whether incorporation by reference can be achieved through the annual preparation and submission of a single CCO Annual Report by a Dual Registrant, the Commission is adding clarifying language to § 3.3(f)(6)(ii). Under new § 3.3(f)(6)(ii), a Dual Registrant may submit a single CCO Annual Report covering the annual reporting requirements relevant to each registration category, provided that: (1) The requirements of § 3.3(e) are clearly addressed and identifiable as they apply to the Dual Registrant in each of its registration capacities; (2) to the extent a section of the CCO Annual Report addresses shared compliance programs, resources, or other elements related to compliance, there is a clear description of the commonality and delineation of any differences; and (3) the Registrant complies with the requirements of § 3.3(f)(1) and (3) to certify and furnish the CCO Annual Report for each of its registrations. Regarding this last requirement, the Commission would expect the Dual Registrant to separately certify the CCO Annual Report with respect to each registration category, even if the same CCO or CEO serves as the certifying officer for each registration.

Subparagraph 3.3(f)(6)(iii) permits Affiliated Registrants to use incorporation by reference within their individually required CCO Annual Reports to address matters shared across related registered legal entities. The Commission believes that providing greater flexibility to Affiliated Registrants may provide a more efficient process in achieving the goals of the CCO Annual Report by leveraging current structures and expertise.

Regarding the extent of incorporation by reference, consistent with the Commission's view that a flexible approach as to form is warranted, the

<sup>70</sup> The Commission also notes that adding "in all material respects" to § 3.3(f)(3) is consistent with the related duty under § 3.3(f)(4) to promptly amend and recertify the CCO Annual Report if "material errors or omissions" in the report are identified (emphasis added).

<sup>67</sup> CCO Rules Adopting Release, 77 FR at 20163.

<sup>68</sup> *Id.*

<sup>69</sup> *Id.* at 20162-3.

Commission is not prescribing a strict requirement. For example, Affiliated Registrants could submit two separate reports, one of which incorporates by reference listed sections of the other. As another example, Affiliated Registrants could create a master report covering multiple affiliates in a manner similar to that described above for Dual Registrants in which information common to the affiliates is provided once in the report and identified as such and then other sections or appendices provide information specific to each affiliate separately. To the extent Affiliated Registrants choose to combine the contents of their individual CCO Annual Reports, the Commission would require the CCO or CEO for each Registrant to certify the applicable contents of the report consistent with § 3.3(f)(3).

The Commission expects that CCOs of Affiliated Registrants who share common compliance program elements be actively engaged in evaluating, assessing, and advising senior management with regard to those elements within their respective duties to a particular Registrant. Accordingly, how a CCO determines to address such common compliance program elements should not undermine the content or representations made in the CCO Annual Report so long as the references are clear and the information is fully accessible to senior management and the Commission.

#### E. Other Comments

##### 1. Volcker Rule

The Commission received two comments regarding the compliance requirements of subpart D of part 75 of the Commission's regulations and their relation to § 3.3. Specifically, FIA/SIFMA requested that the Commission revisit the footnote in the part 75 adopting release that includes the compliance requirements under subpart D of part 75 among the regulations covered by § 3.3(d) and (e).<sup>71</sup> Similarly, ISDA requested that the Commission remove the requirement for an applicable FCM or SD to address Volcker compliance program requirements in its CCO Annual Report.

At this time, the Commission is declining to address the Volcker Rule compliance program requirements issue, as it was not considered in the Proposal. However, the Commission notes that the issue that commenters are raising

requires serious consideration, and it may address the issue in future guidance or rulemakings.

##### 2. Substituted Compliance

The Commission received three comments regarding the applicability of the Proposal to its outstanding comparability determinations for non-U.S. SDs and MSPs. ISDA, the JBA, and Allen & Overy requested clarification from the Commission that the proposed amendments will not have any impact on the current substituted compliance determinations that pertain to § 3.3. The Commission confirms that any existing substituted compliance determinations with respect to § 3.3 are not affected by this rulemaking.

#### IV. Related Matters

##### A. Regulatory Flexibility Act

The Regulatory Flexibility Act ("RFA")<sup>72</sup> requires that agencies consider whether a proposed rule will have a significant economic impact on a substantial number of small entities and, if so, provide a regulatory flexibility analysis of the impact. As noted in the Proposal, the regulations adopted herein would affect FCMs, SDs, and MSPs that are required to be registered with the Commission. The Commission has previously determined that FCMs, SDs, and MSPs are not small entities for purposes of the RFA. The Commission received no comments on the Proposal's RFA discussion. Accordingly, the Chairman, on behalf of the Commission, certifies, pursuant to 5 U.S.C. 605(b), that these regulations will not have a significant economic impact on a substantial number of small entities.

##### B. Paperwork Reduction Act

The Paperwork Reduction Act of 1995 ("PRA")<sup>73</sup> provides that a federal agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid control number issued by the Office of Management and Budget ("OMB"). As discussed in the Proposal, the final rules contain a collection of information for which the Commission has previously received a control number from OMB. The title for this collection of information is OMB control number 3038-0080—Annual Report for Chief Compliance Officer of Registrants. As a general matter, the rules, as adopted: (1) Define the term "senior officer"; (2) clarify the scope of the CCO duties and the content requirements of the CCO

Annual Report; (3) add the Registrant's audit committee as a party that must receive the CCO Annual Report; (4) add a materiality qualifier to the CCO Annual Report certification language; and (5) provide procedural instruction for Dual and Affiliated Registrants in the preparation and submission of CCO Annual Reports that address common information across the same or related legal entities. As discussed in the Proposal and herein, the Commission believes that these regulations, as adopted, will not impose any new information collection requirements that require approval of OMB under the PRA. As such, the final rules do not impose any new burden or any new information collection requirements in addition to those that already exist in connection with the preparation and delivery of the CCO Annual Report pursuant to the Commission's regulations.

##### C. Cost-Benefit Considerations

###### 1. General Considerations

Section 15(a) of the CEA requires the Commission to consider the costs and benefits of its actions before promulgating a regulation under the CEA or issuing certain orders. Section 15(a) further specifies that the costs and benefits shall be evaluated in light of five broad areas of market and public concern: (1) Protection of market participants and the public; (2) efficiency, competitiveness, and financial integrity of futures markets; (3) price discovery; (4) sound risk management practices; and (5) other public interest considerations. The Commission considers the costs and benefits resulting from its discretionary determinations with respect to the section 15(a) factors relative to the status quo baseline—that is existing § 3.3—and how various regulated entities comply with existing § 3.3 today.

The Commission notes that the consideration of costs and benefits below is based on the understanding that the markets function internationally, with many transactions involving U.S. firms taking place across international boundaries; with some Commission registrants being organized outside of the United States; with leading industry members typically conducting operations both within and outside the United States; and with industry members commonly following substantially similar business practices wherever located. While the Commission does not specifically refer to matters of location, the below discussion of costs and benefits refers to

<sup>71</sup> See Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds, 79 FR 5808, 6020 n. 2521 (Jan. 31, 2014).

<sup>72</sup> 5 U.S.C. 601 *et seq.*

<sup>73</sup> 44 U.S.C. 3501 *et seq.*

the effects of the final rule on all activity subject to the final regulation, whether by virtue of the activity's physical location in the United States or by virtue of the activity's connection with or effect on U.S. commerce under CEA section 2(i).<sup>74</sup> In particular, the Commission notes that some registrants subject to § 3.3 are located outside of the United States.

The Commission is adopting amendments to the CCO Rules that: (1) Define the term "senior officer"; (2) clarify the scope of the CCO duties and the content requirements of the CCO Annual Report; (3) add the Registrant's audit committee as a party that must receive the CCO Annual Report; (4) add a materiality qualifier to the CCO Annual Report certification language; and (5) clarify and permit additional procedural methods for Dual and Affiliated Registrants in the preparation and submission of CCO Annual Reports that address common information across the same or related legal entities.

The Proposal requested public comment on the costs and benefits of the proposed regulations, and specifically invited comments on: (1) The extent to which the proposed amendments reduce burdens and costs for Registrants, if at all; (2) whether any of the proposed amendments create any additional burdens or costs for Registrants; (3) whether the nature of, and the extent to which, costs associated with the CCO duties described in § 3.3(d) could change as a result of the adoption of the Proposal, including monetary estimates; (4) what, if any, transition or ongoing costs or savings would result from the adoption of the proposed amendments; (5) whether the proposed amendments to the CCO Annual Report's submission requirements in § 3.3(f)(1) would cause undue burden; and (6) the Commission's preliminary consideration of the costs and benefits associated with the proposed amendments.

Several commenters indirectly addressed the qualitative costs and benefits of the Proposal; however, none included quantitative data or other information in support of a measurable analysis. As such, the Commission is unable to quantify reliably the costs and benefits of this rulemaking. Instead, the Commission gives a qualitative discussion.

As described in the sections above, in support of their comments, several commenters proposed alternative rule text and suggested the Commission provide additional clarification or

guidance. In response to certain comments, the Commission adopted alternatives—particularly with respect to the furnishing and certification requirements of the CCO Annual Report—that the Commission believes will further reduce costs and burdens to Registrants while still providing the Commission with the information it needs to monitor the state of compliance by Registrants.

Informed by commenters, the discussion below considers the rule's costs and benefits generally and in light of the five factors specified in section 15(a) of the CEA.<sup>75</sup>

## 2. Regulation 3.3(d)—Chief Compliance Officer Duties

As discussed above, the Commission amended § 3.3(d) to clarify certain CCO duties. Specifically, the Commission added language to § 3.3(d)(1) to clarify that the CCO's duty with respect to administering policies and procedures is specific to the Registrant's business as an FCM, SD, or MSP, as applicable. As amended, § 3.3(d)(2) incorporates an implied reasonableness standard regarding the duty to resolve conflicts of interest and limits the duty to material conflicts that relate to the Registrant's business as an FCM, SD, or MSP. The Commission amended § 3.3(d)(4) to include the remediation of matters identified "through any means" by the CCO, including the specific discovery methods listed in § 3.3(d)(4). Lastly, the Commission amended § 3.3(d)(4) and (5) to remove the requirement in each provision that the CCO consult with the board of directors or senior officer in connection with resolving noncompliance issues and to clarify that the CCO's duty is to take "reasonable steps to ensure that the registrant" establishes policies and procedures for the remediation and resolution by management of noncompliance issues.

The Commission did not receive any specific comments regarding whether any costs associated with CCO duties would change as a result of the amendments to § 3.3(d). Better Markets opposed several of the proposed amendments to § 3.3(d) that it viewed as

"likely to weaken the CCO regime."<sup>76</sup> The Commission considered Better Markets views and does not believe that the final rules will reduce CCO accountability or marginalize the CCO role. Because the amendments to § 3.3(d) provide greater specificity regarding the role of the CCO and the scope of the CCO's duties while further harmonizing with parallel SEC rules, the Commission believes that the final rule does not impose any additional costs to Registrants, market participants, the markets, or the general public.

The Commission expects the greater clarity provided in the amended rule will reduce burdens on CCOs and improve overall compliance by applying a reasonableness standard to CCO responsibilities rather than deterring effective CCO activities due to concerns of uncertain liability. This greater clarity should also encourage a greater willingness of potential CCOs to vie for and take positions with Registrants. As noted by one commenter, clarifying the CCO's role within a Registrant's overall organization fosters accountability for senior business management and supervisors, and reduces obstacles in attracting and retaining highly qualified professionals to serve as CCOs.<sup>77</sup> Additionally, by further harmonizing the CFTC's and SEC's CCO duties, CCOs of dual SEC-CFTC registrants should be able to fulfill their duties more efficiently and cost effectively.

## 3. Regulation 3.3(e)—Annual Report

In adopting amendments to § 3.3(e), the Commission eliminated the requirement to address "each" applicable CFTC regulatory requirement to which a Registrant is subject in the assessment of the WPPs, since the CCO must still conduct an underlying assessment of the effectiveness of the policies and procedures to meet the requirements of the rule. The Commission further removed the requirement to identify each WPP with respect to each applicable requirement, given that the WPPs are already required to be described in § 3.3(e)(1). Lastly, the Commission clarified that the scope of the resources devoted to compliance that need to be described under § 3.3(e)(4) should be limited to a discussion of resources for the specific activities for which the Registrant is registered.

The comments received for these proposed amendments were generally supportive. For example, one commenter stated that "this Proposal will increase efficiencies by

<sup>75</sup> The final rules add a definition of "senior officer" to § 3.1. As stated in the Proposal, the Commission believes this addition in and of itself had no impact for purposes of determining the costs and benefits of the proposal. Nevertheless, the Commission sought public comment on whether the definition of "senior officer" has any cost and benefit considerations. The Commission received no comments on any cost and benefit considerations of the proposed definition, and, therefore, the analysis of the costs and benefits of the final rules is restricted to the amendments to § 3.3.

<sup>76</sup> Better Markets comment letter.

<sup>77</sup> See FIA/SIFMA comment letter.

<sup>74</sup> 7 U.S.C. 2(i).

streamlining the obligations for market participants that are regulated by both the CFTC and SEC and eliminate unnecessary duplicative policies related to the CCO Annual Report.”<sup>78</sup> One commenter stated that the removal of the requirement-by-requirement assessment from the rule will “allow for more effective conversations to occur between its business partners and the Compliance Department, creating for a more holistic assessment of the Firm’s compliance.”<sup>79</sup> Similarly, another commenter highlighted the benefit to overall compliance of focusing the CCO and compliance personnel on WPPs holistically.<sup>80</sup> Only one commenter expressed a concern that the proposed changes equated to a weakening of the process.<sup>81</sup>

As discussed in the Proposal, in implementing § 3.3(e), the Commission received consistent feedback from Registrants that the exercise of documenting their assessment on a requirement-by-requirement basis was creating a significant economic burden in time and resources. Eliminating the requirement-by-requirement assessment is intended to reduce the burdens on Registrants of producing the CCO Annual Report while maintaining its primary purpose. It is the Commission’s view, supported by commenters, that by reducing the burden associated with this aspect of the CCO Annual Report, CCO and other compliance resources may be better focused on other compliance functions. As discussed in section I.C.2, the final rule does not remove or lessen the CCO’s duties to, among other things, ensure the Registrant is reviewing and assessing the continued soundness of its WPPs. In addition, the amendments harmonize certain CFTC and SEC CCO Annual Report content requirements in an effort to reduce the costs to dual registrants of complying with two regulatory regimes. The Commission believes that the final rule also provides relief for Registrants from resource and time pressures in preparing their CCO Annual Reports.

#### 4. Regulation 3.3(f)—Furnishing the Annual Report and Related Matters

The Commission amended § 3.3(f)(1) to require the CCO to provide the CCO Annual Report to the audit committee or a functionally equivalent body not later than the committee’s next scheduled meeting, but in no event more than 90 days following the furnishing of the

report to the Commission. The Commission also amended the CCO Annual Report’s certification requirement by adding a materiality qualifier to the certification language in § 3.3(f)(3). Lastly, the Commission amended § 3.3(f)(6) to provide procedures for Dual and Affiliated Registrants in the preparation and submission of CCO Annual Reports that address common information across the same or related legal entities.

As discussed above, the Commission received comments from ISDA and FIA/SIFMA asserting that the proposal requiring the senior officer, board of directors, and audit committee to receive the CCO Annual Report would increase operational and regulatory burdens. FIA/SIFMA noted that requiring the boards of directors of SDs that are large, diversified commercial banks to receive the CCO Annual Report would exacerbate current problems associated with the volume of review they must already undertake, further reducing the amount of time they should be allocating to overseeing enterprise risk and strategy. Both commenters believed that the Proposal would add costs, complexities, and possibly, conflicts for Registrants because the deadline to submit the CCO Annual Report to the Commission may not align with board of directors and audit committee meetings, impeding their ability to ensure proper review.

Advocates of adding a materiality qualifier to the CCO Annual Report certification language identified several benefits, including reducing burdens by further harmonizing the Commission’s rule with the SEC’s parallel rule, providing a measure of clarity to CCOs and potential CCOs regarding their own personal liability, and reducing deterrence of highly qualified people from taking or staying in the CCO role.<sup>82</sup> In support of its request for greater flexibility in the preparation of CCO Annual Reports by Affiliated Registrants, FIA/SIFMA noted the benefits of streamlining the overall process.

In response to concerns regarding the proposed CCO Annual Report submission requirements, the Commission has modified § 3.3(f)(1) to accommodate the practicality of audit committee and board meeting schedules. Because the final rule maintains the requirement that either the senior officer or the board of directors receive the CCO Annual Report prior to its submission to the Commission, Registrants should not

have to change existing internal document submission processes for board meetings to comply. As adopted, the final rule adds the audit committee (or equivalent body) as a recipient of the report, but allows for the report to be furnished to the audit committee not later than the next scheduled meeting, but in no event more than 90 days after submission of the report to the Commission is required. Since the rule does not set a timeline for the review of the CCO Annual Report by any of its internal recipients—leaving such matters to the discretion of each Registrant, the Commission believes that any additional costs arising out of the requirement to submit the report to the audit committee should be minimal. The Commission does not believe the final amendments to § 3.3(f)(1), (3) and (6) impose any new costs or burdens since they do not require Registrants to affirmatively undertake new duties or requirements.

As described above and in the Proposal, the Commission believes that the amendments to § 3.3(f) will ensure that the CCO’s findings and recommendations will be distributed to the groups within each Registrant with responsibility for governance and internal controls. Further, the Commission believes the amendments provide greater flexibility and opportunity for Dual and Affiliated Registrants to streamline their CCO Annual Report preparation processes, which may result in a less costly CCO Annual Report.

#### D. Section 15(a) Factors

As noted above, section 15(a) of the CEA specifies that the costs and benefits shall be evaluated in light of five broad areas of market and public concern: (1) Protection of market participants and the public; (2) efficiency, competitiveness, and financial integrity of futures markets; (3) price discovery; (4) sound risk management practices; and (5) other public interest considerations.

##### 1. Protection of Market Participants and the Public

The final rules will continue to protect market participants and the public because they do not fundamentally alter the CCO duties or the annual compliance reporting requirements of § 3.3. While the amendment removing the requirement-by-requirement reporting may reduce the extent of reporting detail, the Commission believes that change will allow the CCO to focus more directly on identifying and describing in the CCO Annual Report material compliance

<sup>78</sup> See NGS comment letter.

<sup>79</sup> See TD Ameritrade comment letter. See also NFA comment letter.

<sup>80</sup> See FIA/SIFMA comment letter.

<sup>81</sup> See Better Markets comment letter.

<sup>82</sup> See FIA/SIFMA, ISDA, and NFA comment letters.

issues and other related matters deserving of greater attention. Accordingly, the Commission believes that the reduction in content requirements will not affect the protection of market participants and the public.

2. Efficiency, Competitiveness, and Financial Integrity of Markets

The Commission believes that the amended CCO Rules will not negatively impact market efficiency, competitiveness, or integrity because each CCO Annual Report addresses internal compliance programs of each Registrant and are not publicly available. The amendments affecting CCO duties only clarify those duties and do not affect the performance of derivatives markets.

3. Price Discovery

The Commission did not identify a specific effect on price discovery as a result of the Proposal because the Proposal did not address any pricing issues. The Commission did not receive any comments on this issue. Thus, the Commission continues to believe that this rulemaking will not have an impact on price discovery.

4. Sound Risk Management Practices

The Commission believes that the final amendments to the CCO duties and CCO Annual Report requirements will not have a meaningful effect on Registrants' risk management practices. The final rules do not directly impact a Registrant's risk management practices because they clarify the scope of the CCO's duties and CCO Annual Report contents, and do not require changes to a Registrant's risk management program.<sup>83</sup> Furthermore, the final amendments to the CCO Annual Report content requirements do not affect the Registrant's obligation to address material noncompliance issues relating to its risk management program in the CCO Annual Report. The Commission believes that including the audit committee and either the board of directors or the senior officer as recipients of the CCO Annual Report may benefit Registrants' overall risk management practices by ensuring that those with overall responsibility for governance and internal controls are informed of the report contents. Finally, the Commission does not believe that the addition of the materiality qualifier to the CCO Annual Report certification language, or the additional procedural mechanisms for addressing common matter across Dual and Affiliated

Registrants impacts Registrants' risk management practices, as they do not impact the CCO Annual Report's content and underlying assessment.

5. Other Public Interest Considerations

The Commission has not identified any other public interest considerations for this rulemaking.

E. Antitrust Considerations

Section 15(b) of the Act requires the Commission to take into consideration the public interest to be protected by the antitrust laws and endeavor to take the least anticompetitive means of achieving the purposes of the Act, in issuing any order or adopting any Commission rule or regulation (including any exemption under section 4(c) or 4c(b)), or in requiring or approving any bylaw, rule, or regulation of a contract market or registered futures association established pursuant to section 17 of the Act.<sup>84</sup> The Commission believes that the public interest to be protected by the antitrust laws is generally to protect competition.

The Commission has reflected on the final rule to determine whether it is anticompetitive and has identified no anticompetitive effects. Because the Commission has determined that the final rulemaking has no anticompetitive effects, the Commission has not identified any less anticompetitive means of achieving the purposes of the Act.

List of Subjects in 17 CFR Part 3

Administrative practice and procedure, Chief compliance officer, Commodity futures, Futures commission merchants, Major swap participants, Registration, Swap dealers, Reporting and recordkeeping requirements.

For the reasons stated in the preamble, the Commodity Futures Trading Commission amends 17 CFR chapter I as follows:

PART 3—REGISTRATION

- 1. The authority citation for part 3 continues to read as follows:

Authority: 5 U.S.C. 552, 552b; 7 U.S.C. 1a, 2, 6a, 6b, 6b-1, 6c, 6d, 6e, 6f, 6g, 6h, 6i, 6k, 6m, 6n, 6o, 6p, 6s, 8, 9, 9a, 12, 12a, 13b, 13c, 16a, 18, 19, 21, and 23.

- 2. In § 3.1, add paragraph (j) to read as follows:

§ 3.1 Definitions.

\* \* \* \* \*

(j) Senior officer. Senior officer means the chief executive officer or other equivalent officer of a registrant.

- 3. In § 3.3, revise paragraphs (d), (e), and (f) to read as follows:

§ 3.3 Chief compliance officer.

\* \* \* \* \*

(d) Chief compliance officer duties. The chief compliance officer's duties shall include, but are not limited to:

(1) Administering each of the registrant's policies and procedures relating to its business as a futures commission merchant, swap dealer, or major swap participant that are required to be established pursuant to the Act and Commission regulations;

(2) In consultation with the board of directors or the senior officer, taking reasonable steps to resolve material conflicts of interest relating to the registrant's business as a futures commission merchant, swap dealer, or major swap participant that may arise;

(3) Taking reasonable steps to ensure compliance with the Act and Commission regulations relating to the registrant's business as a futures commission merchant, swap dealer or major swap participant;

(4) Taking reasonable steps to ensure the registrant establishes, maintains, and reviews written policies and procedures reasonably designed to remediate noncompliance issues identified by the chief compliance officer through any means, including any compliance office review, look-back, internal or external audit finding, self-reporting to the Commission and other appropriate authorities, or complaint that can be validated;

(5) Taking reasonable steps to ensure the registrant establishes written procedures reasonably designed for the handling, management response, remediation, retesting, and resolution of noncompliance issues; and

(6) Preparing and signing the annual report required under paragraphs (e) and (f) of this section.

(e) Annual report. The chief compliance officer annually shall prepare a written report that covers the most recently completed fiscal year of the futures commission merchant, swap dealer, or major swap participant. The annual report shall, at a minimum, contain a description of:

(1) The written policies and procedures of the futures commission merchant, swap dealer, or major swap participant described in paragraph (d) of this section, including the code of ethics and conflicts of interest policies;

(2) The futures commission merchant's, swap dealer's, or major swap participant's assessment of the

<sup>83</sup> See, e.g., 17 CFR 23.600.

<sup>84</sup> 7 U.S.C. 19(b).

effectiveness of its policies and procedures relating to its business as a futures commission merchant, swap dealer or major swap participant;

(3) Areas for improvement, and recommended potential or prospective changes or improvements to its compliance program and resources devoted to compliance;

(4) The financial, managerial, operational, and staffing resources set aside for compliance with respect to the Act and Commission regulations relating to its business as a futures commission merchant, swap dealer or major swap participant, including any material deficiencies in such resources;

(5) Any material noncompliance issues identified and the corresponding action taken; and

(6) Any material changes to compliance policies and procedures during the coverage period for the report.

(f) *Furnishing the annual report and related matters*—(1) *Furnishing the annual report.* (i) Prior to furnishing the annual report to the Commission, the chief compliance officer shall provide the annual report to the board of directors or senior officer of the futures commission merchant, swap dealer, or major swap participant for its review.

(ii) If the futures commission merchant, swap dealer, or major swap participant has established an audit committee (or an equivalent body), then the chief compliance officer shall furnish the annual report to the audit committee (or equivalent body) not later than its next scheduled meeting after the annual report is furnished to the Commission, but in no event more than 90 days after the applicable date specified in paragraph (f)(2) of this section for furnishing the annual report to the Commission.

(iii) A written record of transmittal of the annual report to the board of directors or the senior officer, and audit committee, if applicable, shall be made and maintained in accordance with § 1.31 of this chapter.

(2) *Furnishing the annual report to the Commission.* (i) Except as provided in paragraph (f)(2)(ii) of this section, the annual report shall be furnished electronically to the Commission not more than 90 days after the end of the fiscal year of the futures commission merchant, swap dealer, or major swap participant.

(ii) The annual report of a swap dealer or major swap participant that is eligible to comply with a substituted compliance regime for paragraph (e) of this section pursuant to a comparability determination of the Commission may be furnished to the Commission

electronically up to 15 days after the date on which the comparable annual report must be completed under the requirements of the applicable substituted compliance regime. If the substituted compliance regime does not specify a date by which the comparable annual report must be completed, then the annual report shall be furnished to the Commission by the date specified in paragraph (f)(2)(i) of this section.

(3) *Certification.* The report shall include a certification by the chief compliance officer or chief executive officer of the registrant that, to the best of his or her knowledge and reasonable belief, and under penalty of law, the information contained in the annual report is accurate and complete in all material respects.

(4) *Amending the annual report.* The futures commission merchant, swap dealer, or major swap participant shall promptly furnish an amended annual report if material errors or omissions in the report are identified. An amendment must contain the certification required under paragraph (f)(3) of this section.

(5) *Extensions.* A futures commission merchant, swap dealer, or major swap participant may request from the Commission an extension of time to furnish its annual report, provided the registrant's failure to timely furnish the report could not be eliminated by the registrant without unreasonable effort or expense. Extensions of the deadline will be granted at the discretion of the Commission.

(6) *Incorporation by reference and related registrants*—(i) *Prior reports.* A futures commission merchant, swap dealer, or major swap participant may incorporate by reference sections of an annual report that has been furnished within the current or immediately preceding reporting period to the Commission.

(ii) *Dual registrants.* If a futures commission merchant, swap dealer, or major swap participant is registered in more than one capacity with the Commission, an annual report submitted as one registrant may incorporate by reference sections in the annual report furnished within the current or immediately preceding reporting period as the other registrant. A dual registrant may submit one annual report that addresses the requirements set forth in paragraphs (e), (f)(1) and (f)(3) of this section with respect to each registration capacity.

(iii) *Affiliated registrants.* If a futures commission merchant, swap dealer, or major swap participant controls, is controlled by, or is under common control with, one or more other futures commission merchants, swap dealers, or

major swap participants, and each of the affiliated registrants must submit an annual report, an affiliated registrant may incorporate by reference in its annual report sections from an annual report prepared by any of its affiliated registrants furnished within the current or immediately preceding reporting period. Affiliated registrants may submit one annual report that addresses the requirements set forth in paragraphs (e), (f)(1) and (f)(3) of this section with respect to each affiliated registrant.

\* \* \* \* \*

■ 4. Add appendix C to part 3 to read as follows:

**Appendix C to Part 3—Guidance on the Application of § 3.3(e), Chief Compliance Officer Annual Report Form and Content**

*A. Description of the Registrant's WPPs (§ 3.3(e)(1))*

In acknowledgment of the large number of WPPs that a Registrant implements to comply with CFTC regulations, the Commission understands that for purposes of the CCO Annual Report, specific WPP descriptions may be appropriately brief while still identifying the basic purpose of the policy or procedure and how the policy or procedure operates to achieve that purpose. The CCO Annual Report should include a summary overview that describes the general forms and types of WPPs the Registrant has, such as a compliance manual specific to the Registrant, global corporate manuals or policies, and/or business-unit-specific WPPs that support the applicable regulatory requirements. This summary overview would provide a narrative of the Registrant's system or program of WPPs, how they work as a whole, and how the Registrant generally puts the WPPs into practice as part of its compliance activities. With respect to the COI policy, it is the Commission's view that the CCO should describe the COI policy specific to the Registrant, addressing the specific requirements of § 1.71 or § 23.605 of this chapter, as applicable.

*B. Assessment of the Effectiveness of the Policies and Procedures (§ 3.3(e)(2))*

The Commission expects a CCO Annual Report to contain a comprehensive discussion of: the assessment process; and the results of the effectiveness assessment. The regulation does not dictate the form or manner for the effectiveness assessment. Rather, the Commission would expect each Registrant to follow a process and present the resulting assessment in a form and manner that is appropriate for the size and complexity of the Registrant's applicable business activities and structure. While § 3.3(e)(2) no longer has a "requirement-by-requirement" standard, the CCO Annual Report should address all of the general areas of regulation applicable to the Registrant.

*C. Areas for Improvement and Recommended Changes (§ 3.3(e)(3))*

1. Section 3.3(e)(3) requires two components in the CCO Annual Report: an

identification and discussion of each area that needs improvement; and a discussion of what changes are recommended to address each area needing improvement. In addressing these two elements, the CCO Annual Report should include, as applicable: A discussion of why the particular area needs improvement; a discussion of the proposed improvements and the time frame for their implementation; and a cross-reference to the regulation that a recommended change would address.

2. In general, identifying areas in need of improvement and recommending steps to effect those improvements should be a core function of compliance. Accordingly, a CCO Annual Report that makes no recommendations for changes or improvements to the compliance program may raise concerns about the adequacy of the compliance program review intended by the CCO Annual Report process. Moreover, there should be continuity from one reporting cycle to the next, such that where a previous CCO Annual Report discussed future changes or improvements that were being considered or planned, subsequent CCO Annual Reports should discuss the outcomes of the changes that were implemented during the most recent scope period, any monitoring or testing of those changes, whether any compliance issues arose from the changes and, if there were any issues, how those issues were handled. While this section may address improvements to the compliance program that have already been completed, the Commission believes that this section primarily should discuss recommended improvements in process and/or future plans to improve the Registrant's compliance program or resources devoted to compliance.

#### *D. Resources Set Aside for Compliance (§ 3.3(e)(4))*

1. The resources description required by § 3.3(e)(4) should be appropriate for assisting the Registrant's senior management and the CFTC in assessing whether sufficient resources are dedicated to compliance. Accordingly, the description should include the following types of information: the budget allocated to the compliance department of the Registrant for compliance with the CEA and Commission regulations; full-time compliance staffing levels for such compliance activities; partially allocated staff counts (if applicable), with information on how much of such employees' time is devoted to the Registrant's compliance matters that are subject to CFTC oversight; an explanation of managerial resources (the explanation should clearly identify the division between staffing resources and management resources devoted to compliance); general infrastructure information (e.g., computers, compliance-oriented software, technology infrastructure, etc.); and if applicable, a description of the use of third party vendors or outsourcing for compliance activities. In most cases, to effectively inform the board of directors or senior officer and the Commission, the description should include quantifiable information for the financial, managerial, operational, and staffing resources allocated to compliance with the CEA and Commission regulations.

2. The Commission understands that a discussion of specific compliance budget allocations may not be as straightforward as described above depending on the size and complexity of the Registrant's compliance program and the extent to which the Registrant's compliance resources may be shared for other non-CFTC regulated business activities. The purpose of the CCO Annual Report requirement is to convey to senior management and the CFTC a clear understanding of the resources the Registrant has set aside for compliance with the CEA and Commission regulations. While some of the compliance resources used in a Registrant's CFTC compliance-related program may be used for compliance activities in other parts of a larger corporate enterprise, this sharing of resources does not negate the Registrant's obligation to discuss how the Registrant's compliance program is being resourced. For those instances where compliance resources are shared, it is recognized that the description of the shared resources may reasonably be more general in nature, providing approximations and estimates based on expected needs. However, the Commission expects that the CCO Annual Report will still address shared resources in as much detail as is necessary to convey the information needed to assess the overall compliance activities of the Registrant.

3. Section 3.3(e)(4) also requires that the CCO Annual Report include a discussion of any material deficiencies in compliance resources. If there have been reductions in the compliance program of the Registrant since the prior reporting period, for example, if there has been a reduction in compliance staff, a significant compliance budget decrease, or the Registrant initiated significant new business activities without a corresponding increase in compliance resources, the CCO Annual Report should include an explanation of why the compliance resources are not deficient in light of the changes. If there are no material deficiencies in the resources devoted to compliance, the Commission recommends that the CCO Annual Report contain an express statement to that effect so that the recipients of the report can see that the requirement was assessed.

#### *E. Material Noncompliance Issues (§ 3.3(e)(5))*

The CCO Annual Report should include an explanation of the standard the Registrant used to determine a non-compliance event's materiality. In addition, this section of the CCO Annual Report should contain a description of each material non-compliance issue identified either through self-assessment procedures conducted within the Registrant, or noted by any external entities which conducted a review of the Registrant (such as a designated self-regulatory organization). The description should also include the corresponding actions taken, described in reasonable detail, as well as specific references to the Commission regulation or regulations that are implicated by the non-compliance event. Specifically, the Commission recommends that the CCO Annual Report include a discussion of the

Registrant's deliberations on a course of remediation, how the implementation of the remediation is being or was executed, any follow-up testing of the remediation, and any noteworthy results from such testing. Additionally, the Commission recommends that CCOs consider including an overview of how the CCO or compliance department handles and tracks non-compliance events in general.

#### *F. Material Changes to WPPs (§ 3.3(e)(6))*

When describing any material changes to the WPPs, a description of the standard of materiality used should be provided. This description will provide meaningful context for any reported changes to the WPPs.

Issued in Washington, DC, on August 21, 2018, by the Commission.

**Christopher Kirkpatrick,**  
*Secretary of the Commission.*

**Note:** The following appendices will not appear in the Code of Federal Regulations.

### **Appendices to Chief Compliance Officer Duties and Annual Report Requirements for Futures Commission Merchants, Swap Dealers, and Major Swap Participants; Amendments—Commission Voting Summary and Chairman's Statement**

#### **Appendix 1—Commission Voting Summary**

On this matter, Chairman Giancarlo and Commissioners Quintenz and Behnam voted in the affirmative. No Commissioner voted in the negative.

#### **Appendix 2—Statement of Chairman J. Christopher Giancarlo**

As part of the CFTC's Project KISS efforts, this final rule will streamline and clarify a Chief Compliance Officer's (CCO) obligations, as well as harmonize certain provisions with the Securities and Exchange Commission's (SEC) rules. Clarifying the role and responsibilities of the CCO should enable greater accountability and improve overall compliance, as well as reduce burdens on CCOs and uncertainty for registrants. The rule continues to impose a duty on CCOs to resolve matters but within the practical limits of their position at the CFTC-registered entity. The rule also continues to impose a duty for the CCO to undertake an annual review but reduces the burdens associated with the review, which will allow the CCO to devote more time and resources to compliance activities at the registrant. In addition, further harmonizing definitions and CCO duties of dual CFTC-SEC registrants should improve efficiency and further reduce the burdens on CCOs.

I would like to thank CFTC staff for their efforts. I would also like to thank Commissioners Quintenz and Behnam for their support.

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