



6351-01-P

## **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; Amendments**

**AGENCY:** Commodity Futures Trading Commission.

**ACTION:** Proposed rule.

**SUMMARY:** The Commodity Futures Trading Commission (“Commission” or “CFTC”) is proposing to amend 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 and furnishing to the Commission an annual report containing an assessment of the Registrant’s compliance activities.

**DATES:** Comments must be received on or before **[INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER]**.

**ADDRESSES:** You may submit comments, identified by RIN 3038-AE56, by any of the following methods:

- CFTC website: <https://comments.cftc.gov>. Follow the instructions for submitting comments through the Comments Online process on the website.
- Mail: Christopher Kirkpatrick, Secretary of the Commission, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW, Washington, DC 20581.

- Hand Delivery/Courier: Same as Mail, above.
- Federal eRulemaking Portal: <http://www.regulations.gov>. Follow the

instructions for submitting comments.

Please submit your comments using only one method.

All comments must be submitted in English, or if not, accompanied by an English translation. Comments will be posted as received to [www.cftc.gov](http://www.cftc.gov). You should submit only information that you wish to make available publicly. If you wish the Commission to consider information that is exempt from disclosure under the Freedom of Information Act (“FOIA”),<sup>1</sup> a petition for confidential treatment of the exempt information may be submitted according to the procedures set forth in § 145.9 of the Commission’s regulations.<sup>2</sup>

The Commission reserves the right, but shall have no obligation, to review, pre-screen, filter, redact, refuse or remove any or all of your submission from [www.cftc.gov](http://www.cftc.gov) that it may deem to be inappropriate for publication, such as obscene language. All submissions that have been redacted or removed that contain comments on the merits of the rulemaking will be retained in the public comment file and will be considered as required under the Administrative Procedure Act and other applicable laws, and may be accessible under the FOIA.

**FOR FURTHER INFORMATION CONTACT:** Eileen T. Flaherty, Director, 202-418-5326, [eflaherty@cftc.gov](mailto:eflaherty@cftc.gov); Erik Remmler, Deputy Director, 202-418-7630, [eremmler@cftc.gov](mailto:eremmler@cftc.gov); Laura Gardy, Associate Director, 202-418-7645, [lgardy@cftc.gov](mailto:lgardy@cftc.gov); Pamela M. Geraghty, Special Counsel, 202-418-5634, [pgeraghty@cftc.gov](mailto:pgeraghty@cftc.gov); or Fern B.

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<sup>1</sup> 5 U.S.C. 552.

<sup>2</sup> 17 CFR 145.9. Commission regulations referred to herein are found at 17 CFR chapter I.

Simmons, Special Counsel, 202-418-5901, [fsimmons@cftc.gov](mailto:fsimmons@cftc.gov), Division of Swap Dealer and Intermediary Oversight, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW, Washington, DC 20581.

## **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>3</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>4</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>5</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>6</sup> In 2012, the Commission adopted regulations 3.3(d) through (f) implementing the duties described in CEA sections 4d(d) and 4s(k).<sup>7</sup>

#### **B. Consistency With SEC Rules**

Using language identical to CEA section 4s(k), the Dodd-Frank Act amended the Securities Exchange Act of 1934 (“Exchange Act”) by adding section 15F(k) to establish the same CCO requirements for security-based swap dealers and major security-based

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<sup>3</sup> See Dodd-Frank Act, Public Law 111-203, 124 Stat. 1376 (2010).

<sup>4</sup> 7 U.S.C. 6d(d) and 6s(k)(1).

<sup>5</sup> 7 U.S.C. 6s(k)(2) and (3).

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

<sup>7</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) (“CCO Rules Adopting Release”). For purposes of this release, these rules will be referred to as the “CCO Rules.”

swap participants (collectively, “SEC Registrants”).<sup>8</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 and comparability.<sup>9</sup>

The SEC initially proposed rule 15Fk-1 to implement CCO requirements and duties for SEC Registrants in July 2011.<sup>10</sup> In May 2013, after the CFTC adopted the CCO Rules, the SEC re-opened the comment period for its outstanding Dodd-Frank Act Title VII rulemakings, including rule 15Fk-1.<sup>11</sup> In its reopening release, the SEC sought comment on, among other things: (1) the relationship of the proposed SEC rules to any parallel CFTC requirements; and (2) the extent to which the SEC should emphasize consistency with the CFTC rules or should tailor its rules to the security-based swap market.<sup>12</sup> Comments received by the SEC largely urged the SEC to harmonize its business conduct rules, including rule 15Fk-1, with those of the CFTC because the industry had already implemented the CFTC’s regulations.<sup>13</sup> Specifically, with respect to supervision and CCO obligations, commenters urged that the SEC’s final rules “be informed by industry experience complying with . . . the CFTC internal business conduct

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<sup>8</sup> 15 U.S.C. 78o-10(k).

<sup>9</sup> Public Law 111-203, 124 Stat. 1376, 1641-1642 (codified at 15 U.S.C. 8302(a)(1)-(2)).

<sup>10</sup> See Business Conduct Standards for Security-Based Swap Dealers and Major Security-Based Swap Participants, 76 FR 42396 (proposed Jul. 18, 2011).

<sup>11</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>12</sup> Id. at 30802.

<sup>13</sup> Business Conduct Standards for Security-Based Swap Dealers and Major Security-Based Swap Participants, 81 FR 29960, 29964 (May 13, 2016) (“SEC Adopting Release”).

standards” among others.<sup>14</sup> A number of comments also suggested specific conforming modifications to the SEC’s proposed rules.<sup>15</sup>

SEC staff continued to consult with CFTC staff leading up to adoption of the SEC’s business conduct standards rules, which became effective July 12, 2016.<sup>16</sup> As explained in the SEC Adopting Release, the SEC modified the proposed rules “to harmonize with CFTC requirements to create efficiencies for entities that have already established infrastructure for compliance with analogous CFTC requirements” where such modifications “will continue to provide the protections (as explained in the context of the particular rule) that the rules were intended to accomplish.”<sup>17</sup>

### C. Further Harmonization

Although the SEC’s CCO rules are largely harmonized with the CFTC’s corresponding regulations, rule 15Fk-1 as adopted differs in several respects. Based on CFTC staff experience in implementing the CCO Rules, review of the comments to the proposed SEC rule 15Fk-1, and discussions with SEC staff, the Commission believes that some of the differences adopted by the SEC are beneficial for market participants and regulatory oversight.

The CCO Rules, among other things, seek to ensure that the CCO is actively engaged in compliance activities with the appropriate authority, resources, and access to the board of directors or senior officer to administer the firm’s compliance activities.<sup>18</sup>

As described below, the proposed amendments to the CCO Rules preserve these

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<sup>14</sup> Id. at 29964 n.31.

<sup>15</sup> Id.

<sup>16</sup> 17 CFR 240.15Fk-1. See SEC Adopting Release, 81 FR at 29960.

<sup>17</sup> SEC Adopting Release, 81 FR at 29964.

<sup>18</sup> See, e.g., CCO Rules Adopting Release, 77 FR at 20161-2.

objectives and should increase efficiencies, reduce regulatory burden, particularly for dual registrants, and further clarify the scope of CCO duties.

## **II. The Proposal**

### **A. Regulation 3.1 – Definitions**

The Commission proposes to add a definition of “senior officer” to § 3.1 to provide greater clarity regarding the CCO reporting line required by CEA section 4s(k)(2)(A) and § 3.3(a)(1) of the Commission’s regulations.<sup>19</sup> The Commission has not previously formally defined this term for purposes of the CCO Rules. However, Commission staff has generally interpreted this term to refer to a Registrant’s most senior officer, typically the chief executive officer or the equivalent. This interpretation is consistent with the SEC’s definition of “senior officer” in SEC rule 15Fk-1(e)(2). Accordingly, the Commission is proposing to define “senior officer” in new paragraph (j) to § 3.1 as “the chief executive officer or other equivalent officer of a registrant.”

This definition is in keeping with the Commission’s continued belief that, as stated in the CCO Rules Adopting Release, a “direct reporting line” from the CCO to the board of directors or highest executive officer ensures CCO independence.<sup>20</sup> The “chief executive officer” is typically the highest executive level, but the definition includes the phrase “other equivalent officer” to acknowledge that a firm may have a different title for the highest executive officer.

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<sup>19</sup> 7 U.S.C. 6s(k)(2)(A); 17 CFR 3.3(a)(1).

<sup>20</sup> See CCO Rules Adopting Release, 77 FR at 20160. As noted in the release, reporting to a senior officer of a division of a larger company would be appropriate only when that division is registered as a swap dealer (i.e., a limited swap dealer designation under 17 CFR 1.3(ggg)(3)). Id.

Request for comment: The Commission requests comment regarding the proposed definition in § 3.1. The Commission specifically requests comment on the following questions:

- Should the proposed definition for “senior officer” be revised? If yes, please provide alternative suggestions.
- Should other definitions be added?

B. Regulation 3.3(d) – Chief Compliance Officer Duties

Paragraph (d) of § 3.3 implements the CCO duties required by CEA section 4s(k). Generally, paragraph (d) requires the CCO to: (1) establish and administer policies and procedures, including those related to ensuring compliance and remediating noncompliance issues; (2) resolve any conflicts of interest; and (3) prepare the CCO Annual Report. Based on the practical experience gained from four years of implementation, the Commission has determined that certain CCO Rules could be revised to more accurately convey the Commission’s intent with respect to the scope of the CCO’s duties and to further harmonize with the SEC’s recently finalized CCO rules. In this regard, the proposed amendments are intended to maintain and clarify the underlying goal of the CCO’s active engagement in compliance monitoring while reducing regulatory burdens that provide limited corresponding benefit.<sup>21</sup>

1. Regulation 3.3(d)(1) – Duty to Administer Compliance Policies and Procedures

Paragraph (d)(1) of § 3.3 implements CEA section 4s(k)(2)(D), which requires a CCO to “be responsible for administering each policy and procedure that is required to be

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<sup>21</sup> See CCO Rules Adopting Release, 77 FR at 20161-2.

established pursuant to this section.”<sup>22</sup> The current text of § 3.3(d)(1) states that the CCO’s duties include “administering the registrant’s policies and procedures reasonably designed to ensure compliance with the Act and Commission regulations.”<sup>23</sup> The Commission is proposing to amend § 3.3(d)(1) to require the CCO to administer “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.”

The proposed change clarifies that the CCO is responsible for administering the policies and procedures specifically related to the Registrant’s business as a SD, MSP, or FCM, as applicable, not all of the Registrant’s business that may otherwise be subject to CFTC regulation. Further, the proposed change more closely tracks the language of CEA section 4s(k)(2)(D) and is consistent with the Commission’s stated intent when finalizing the CCO Rules.<sup>24</sup> Finally, the amended rule text more closely tracks the language of the SEC’s parallel rule<sup>25</sup> and should alleviate concerns regarding consistency with the SEC’s interpretation of identical statutory language as it applies to dual CFTC Registrants and SEC Registrants.

## 2. Regulation 3.3(d)(2) – Resolving Conflicts of Interest

Paragraph (d)(2) of § 3.3 requires the CCO to, in consultation with the board of directors or the senior officer, resolve any conflicts of interest that may arise. The

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<sup>22</sup> 7 U.S.C. 6s(k)(2)(D).

<sup>23</sup> 17 CFR 3.3(d)(1).

<sup>24</sup> CCO Rules Adopting Release, 77 FR at 20158. (“[T]he Commission 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>25</sup> 17 CFR 240.15Fk-1(b)(4).

Commission is proposing to modify § 3.3(d)(2) to clarify that the CCO must take “reasonable steps” to resolve conflicts. This proposed change makes explicit an implied reasonableness standard and recognizes that resolution of non-material conflicts need not always require the CCO’s direct expertise or directly involve the board of directors or senior officer.<sup>26</sup>

The Commission is of the view that a CCO’s duty to resolve conflicts of interest should not be interpreted to require the CCO to personally resolve every potential conflict of interest that may arise or require consultation with the board of directors or senior office. If strictly interpreted, the current rule text creates an undue burden on CCOs, likely taking them away from more important compliance activities. The proposed changes are intended to clarify 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>27</sup> With this amendment, the CCO and his or her resources may more effectively engage in working to resolve conflicts practically and within normal business operations procedures.

Similarly, the SEC in its adopting release noted that the CCO’s role in resolving conflicts of interest would likely include the recommendation of actions to resolve the conflict, as well as the escalation and reporting of issues related to resolution, but not executing the business decisions to ultimately resolve the conflict.<sup>28</sup> The SEC articulated

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<sup>26</sup> The CEA and Exchange Act require CCO’s to “in consultation with the board of directors, a body performing a function similar to the board, or the senior officer of the organization, resolve any conflicts of interest that may arise.” 7 U.S.C. 6s(k)(2)(C) and 15 U.S.C. 78o-10(k)(2)(C).

<sup>27</sup> See 7 U.S.C. 6s(k)(3)(A)(ii) (requiring policies and procedures to include conflicts of interest policies).

<sup>28</sup> See SEC Adopting Release, 81 FR at 30057 (stating that “the primary responsibility for the resolution of conflicts generally lies with the business units . . .”).

this understanding in its final rule 15Fk-1(b)(3) by requiring a CCO to “take reasonable steps” to resolve conflicts of interests. The Commission believes it is appropriate to incorporate this language into § 3.3(d)(2) to more accurately reflect its interpretation of the statutory requirement.

### 3. Regulation 3.3(d)(3) – Ensuring Compliance

The Commission proposes to amend paragraph (d)(3) of § 3.3 to incorporate further guidance regarding the extent of a CCO’s compliance duties. Current § 3.3(d)(3) effectuates CEA section 4s(k)(2)(E)<sup>29</sup> by requiring CCOs to take “reasonable steps to ensure compliance with the Act and Commission regulations relating to the swap dealer’s or major swap participant’s swaps activities, or to the futures commission merchant’s business as a futures commission merchant.”<sup>30</sup> The Commission proposes to amend § 3.3(d)(3) by clarifying that the CCO’s duty in this subsection includes “ensuring the registrant establishes, maintains and reviews written policies and procedures reasonably designed to achieve compliance” with the Act and Commission regulations. This change is consistent with the SEC’s parallel rule.<sup>31</sup>

When finalizing § 3.3(d)(3), the Commission intended to address commenter concerns that fully “ensuring compliance” with the CEA could be an impracticable standard for CCOs and that the regulatory responsibility for ensuring compliance is ultimately borne by the registrant.<sup>32</sup> The Commission modified the proposal in the final

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<sup>29</sup> 7 U.S.C. 6s(k)(2)(E) imposes a duty on CCOs to “ensure compliance with this Act [CEA] (including regulations) relating to swaps, including each rule prescribed by the Commission under this section.”

<sup>30</sup> 17 CFR 3.3(d)(3).

<sup>31</sup> 17 CFR 240.15Fk-1(b)(2).

<sup>32</sup> See CCO Rules Adopting Release, 77 FR at 20162.

rule by limiting the CCO duties to taking “reasonable steps to ensure compliance” rather than simply “ensure compliance.”<sup>33</sup>

Notwithstanding the change made to the final CCO Rules, during the more than four years of implementing § 3.3(d)(3), CCOs and their representatives have expressed concern about the uncertainty as to the breadth of their required authority under the rule. Accordingly, by amending § 3.3(d)(3), the Commission intends to address uncertainty caused by the current text of § 3.3(d)(3) by specifically identifying the CCO’s duties with regard to compliance policies and procedures.<sup>34</sup> The amended language also will further harmonize with the SEC’s final interpretation of the role of the CCO.<sup>35</sup>

#### 4. Regulations 3.3(d)(4) and (5) – Remediation of Noncompliance Issues

Paragraphs (d)(4) and (5) currently require a CCO to establish procedures, in consultation with the board of directors or the senior officer, for (1) the remediation of noncompliance issues identified by the CCO and (2) the handling, management response, remediation, retesting, and closing of noncompliance issues.<sup>36</sup> The Commission proposes to remove the consultation requirement in paragraphs (d)(4) and (5) as superfluous and clarify that the policies and procedures be “reasonably designed” to achieve the stated purpose. In removing the consultation requirement, the Commission acknowledges that

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<sup>33</sup> In making this modification, the Commission considered the SEC’s similar interpretation of the duty to ensure compliance in its proposed rule effectuating identical statutory language. See id.

<sup>34</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, 70883 (proposed Nov. 19, 2010) (“Underlying all of these duties are two fundamental acknowledgements: The chief compliance officer can only ensure the registrant’s compliance to the full capacity of an individual person, and the duties of the chief compliance officer do not elevate the position above the board of directors, or otherwise contradict basic and well-established tenets of law regarding the allocation of responsibility within a business association.”).

<sup>35</sup> In finalizing its rules for SEC Registrants, the SEC departed from its proposed language and similarly concluded that, “it is the responsibility of the SBS Entity, not the CCO in his or her personal capacity, to establish and enforce required policies and procedures.” See SEC Adopting Release, 81 FR at 30056.

<sup>36</sup> 17 CFR 3.3(d)(4) and (5).

in carrying out their duties, a CCO should manage and remediate compliance issues by consulting, as appropriate, with business lines, senior management, the board of directors, and independent review groups.

Furthermore, the Commission is proposing to amend § 3.3(d)(4) to include remediating matters identified “through any means” by the chief compliance officer in addition to the specific detection methods listed in the rule text. This change addresses a concern discussed in the SEC Adopting Release that the list of specific methods in the current regulatory text could be viewed as a limit on noncompliance event discovery methods.<sup>37</sup> The flexibility added by this change is particularly meaningful given advances in automated compliance monitoring technology.

Request for comment: The Commission requests comment regarding the proposed amendments to the CCO duties in § 3.3(d). The Commission specifically requests comment on the following questions:

- Are the proposed revisions to the CCO duties appropriate? If not, what modifications to the duties should be made?
- Do the proposed amendments create added efficiencies for dual CFTC and SEC Registrants?
- To what extent do the proposed amendments reduce burdens and costs for Registrants?
- Do any of the proposed amendments create any additional burdens or costs for Registrants?

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<sup>37</sup> See SEC Adopting Release, 81 FR at 30056.

- Should the Commission revise any other requirements under § 3.3(d)? If so, which ones and why?

- Should the Commission seek to further harmonize the requirements under § 3.3(d) with parallel SEC requirements?

C. Proposed Amendments to Regulations 3.3(e) and (f) – CCO Annual Reporting

CEA section 4s(k)(3) requires the CCO to annually prepare and sign the CCO Annual Report and Commission § 3.3(e) and (f) implement this requirement.<sup>38</sup> The Commission proposes to revise, reorganize, and clarify § 3.3(e) and (f) to further reduce burdens to Registrants, incorporate related proposed amendments to § 3.3(d), and further harmonize with the SEC’s parallel rules. When the Commission proposed § 3.3(e) and (f), it stated that the intended purposes for these rules were to: (1) promote compliance behavior through periodic self-evaluation; and (2) inform the Commission of possible compliance weaknesses.<sup>39</sup> Further, in the adopting release, the Commission noted that the rules will assist the Registrant and the Commission in determining whether the Registrant remains in compliance with the CEA and Commission regulations.<sup>40</sup> The Commission is reaffirming these stated purposes and believes that the proposed revisions will more effectively further these goals.

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<sup>38</sup> 7 U.S.C. 6s(k)(3) and 17 CFR 3.3(e) and (f).

<sup>39</sup> 75 FR at 70883.

<sup>40</sup> See CCO Rules Adopting Release, 77 FR at 20193 (“The annual compliance report 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. It also will assist the Commission in determining whether the registrant remains in compliance with the CEA and the Commission’s regulations . . .”).

1. Regulation 3.3(e) – Annual Report

Paragraph (e)(1) of § 3.3 implements CEA section 4s(k)(3)(A)(ii) and requires the CCO Annual Report to include a description of the Registrant’s written policies and procedures (“WPPs”), including the code of ethics and conflicts of interest policies. The Commission is proposing to amend § 3.3(e)(1) to further clarify which WPPs must be described in the CCO Annual Report by referencing the WPPs described in paragraph (d), as amended.

Paragraphs (e)(2)(i), (ii), and (iii) of § 3.3 currently require the CCO Annual Report to identify the Registrant’s WPPs designed to reasonably comply with the CEA and Commission regulations, assess the effectiveness of the WPPs, and discuss any areas of improvement and recommended changes or improvements to the Registrant’s compliance program.<sup>41</sup> The current language of § 3.3(e)(2) applies these three requirements to each applicable CFTC regulatory requirement to which the Registrant is subject. In other words, for each applicable CFTC requirement the CCO Annual Report must identify a WPP, assess the WPP, and discuss related areas of improvement.

After adoption of the rule, Commission staff received industry feedback indicating that the amount of time and resources needed for the review described above makes the process burdensome when compared to the intrinsic value of this portion of the report, particularly given that many of the WPPs do not change from year to year.<sup>42</sup>

Commission staff has also observed that many of the CCO Annual Reports provide the

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<sup>41</sup> See 17 CFR 3.3(e)(2)(i)-(iii).

<sup>42</sup> To alleviate some of this burden, Commission staff indicated in guidance that a chart may provide an appropriate mechanism for efficiently addressing the requirements of § 3.3(e)(2) for purposes of the CCO Annual Report. CFTC Staff Advisory No. 14-153 at 6 (Dec. 22, 2014) (“CCO Annual Report Advisory”). However, the Commission believes that while use of a chart may streamline the presentation of information, it does not fundamentally change the burden of the underlying review and assessment.

detail required in a rote manner, but contain limited substantive discussion regarding areas of improvement and recommended changes to the compliance program, especially where such modifications may relate to the remediation of material noncompliance issues.<sup>43</sup> This observation raises concerns as to whether the CCO Annual Report requirements are promoting an active, on-going self-evaluation or, instead, encouraging a more limited, “check-the-box” appraisal.

Based on the foregoing, the Commission is proposing to amend § 3.3(e)(2) to eliminate the requirement to address “each applicable requirement under the Act and Commission regulations” and make other conforming edits. In addition, § 3.3(e)(2)(i) is being deleted because Registrants are already required by § 3.3(e)(1) to describe their WPPs.<sup>44</sup> The Commission believes that the intent of CEA section 4s(k)(3)(A) and the purpose of the CCO Annual Report may be met where Registrants provide summaries of their WPPs coupled with a detailed discussion of their annual assessment and recommended improvements.<sup>45</sup>

As a related change, § 3.3(f) specifically contains the full requirements regarding delivery of the CCO Annual Report. To eliminate confusion and unnecessary duplication, the Commission proposes to amend § 3.3(e) to remove the duplicative text regarding the duty to furnish the CCO Annual Report.

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<sup>43</sup> See 17 CFR 3.3(e)(5).

<sup>44</sup> Although the requirement to identify WPPs that are reasonably designed to ensure compliance is being deleted, the Commission notes that it can gain access to each of the Registrant’s policies and procedures through the Commission’s authority to request the production of books and records under § 1.31, 17 CFR 1.31.

<sup>45</sup> Consistent with the CCO Annual Report Advisory, Registrants may continue to use a chart to present assessment and review findings, as well as other information required by § 3.3(e). However, the use of a chart does not alleviate the requirement to provide meaningful, substantive discussion where required. CCO Annual Report Advisory at 9-11.

The Commission is also proposing to amend § 3.3(e)(4), which requires that the Registrant describe in the CCO Annual Report its financial, managerial, operational, and staffing resources set aside for compliance with the Act and Commission regulations. Commission staff has received a number of questions regarding whether the description need only cover resources for the activities for which the Registrant is registered or must also address other activities covered by the Act and Commission regulations. The Commission is proposing to amend § 3.3(e)(4) to clarify that the discussion is limited to resources allocated to the specific activities for which the Registrant is registered. It is the Commission's view that the CCO Annual Report is meant to be a report regarding a Registrant's business as an FCM, SD, or MSP, and therefore information need only be included in the CCO Annual Report to the extent it is related to, or impacts, that part of the Registrant's business.

The changes to § 3.3(e)(2) in this proposal closely parallel SEC rule 15Fk-1(c)(2).<sup>46</sup> The Commission believes that greater efficiencies can be achieved for dual CFTC and SEC Registrants when the structure and content requirements for both CCO Annual Reports is consistent.

Finally, to fully implement the amendments to § 3.3(e), the Commission is proposing to renumber current § 3.3(e)(3) as § 3.3(e)(6), to account for the proposed renumbering of the other content requirements in current § 3.3(e)(2).

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<sup>46</sup> See SEC Adopting Release, 81 FR at 30058; 17 CFR 240.15Fk-1(c)(2)(A).

2. Regulation 3.3(f) – Furnishing the annual report to the Commission

CEA section 4s(k)(3)(B) requires the CCO Annual Report to, among other things, be furnished to the Commission and include a certification that the report is accurate and complete. Paragraph (f) of § 3.3 implements this requirement.

Section 3.3(f)(1) only requires delivery of the CCO Annual Report to the board of directors or the senior officer of the Registrant in addition to the Commission. The Commission is proposing to amend § 3.3(f)(1) to require a Registrant to provide its CCO Annual Report to its audit committee (or equivalent body), the board of directors, and the senior officer prior to furnishing it to the Commission.<sup>47</sup> This amendment would align this requirement with that of the SEC’s corresponding rule, 15Fk-1(c)(2)(ii)(B). In requiring the SEC CCO Annual Report to be delivered to the audit committee, the SEC stated that requiring submission to the audit committee, in addition to the board and the senior officer, further ensures that all groups with overall responsibility for governance and internal controls remain informed of the SEC Registrant’s compliance program.<sup>48</sup> The Commission agrees with this policy goal and also believes that further aligning our rules provides for greater efficiency.

Request for comment: The Commission requests comment regarding the proposed amendments to the CCO Annual Report’s requirements in § 3.3(e) and (f). The Commission encourages all comments, including background information, actual market examples, best practice principles, and estimates of any asserted costs and expenses.

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<sup>47</sup> Per its longstanding position, the Commission is reiterating that in the event a Registrant does not have a board of directors, under the proposed amendment, the CCO Annual Report would be furnished to the senior officer and audit committee, or other equivalent body or group performing the auditing function.

<sup>48</sup> SEC Adopting Release, 81 FR at 30059.

Regarding the proposed CCO Annual Report amendments, the Commission specifically requests comment on the following questions:

- Are the proposed amendments to the CCO Annual Report’s content requirements in § 3.3(e) appropriate? If not, what modifications to the content requirements should be made?
- What, if any, transition or ongoing costs or savings would result from such changes? Please provide details and estimates regarding any asserted costs or savings.
- Would the proposed amendments to the CCO Annual Report’s submission requirements in § 3.3(f)(1) cause undue burden? Is it appropriate for the audit committee to receive the CCO Annual Report?
- Should the Commission make any other changes to § 3.3(f) to further harmonize with the SEC?

### **III. Related Matters**

#### **A. Regulatory Flexibility Act**

The Regulatory Flexibility Act (“RFA”)<sup>49</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. The proposed amendments define the term “senior officer;” clarify the scope of a CCO’s duties and the content requirements of the CCO Annual Report; and modify the CCO Annual Report delivery requirement. The proposed amendments would affect FCMs, SDs, and MSPs that are required to be registered with the Commission. The Commission has previously established certain definitions of “small entities” to be used in evaluating the impact of its

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<sup>49</sup> 5 U.S.C. 601 et seq.

regulations on small entities in accordance with the RFA, and has previously determined that FCMs, SDs, and MSPs are not small entities for purposes of the RFA.<sup>50</sup> Therefore, the Commission believes that the amendments to the CCO Rules would not have a significant economic impact on a substantial number of small entities. Accordingly, the Acting Chairman, on behalf of the Commission, hereby certifies, pursuant to 5 U.S.C. 605(b), that the proposed amendments 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>51</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”). The collection of information related to this proposed rule is OMB control number 3038–0080—Annual Report for Chief Compliance Officer of Registrants. As a general matter, the proposed amendments to the CCO Rules: (1) define the term “senior officer”; (2) clarify the scope of the CCO duties and the content requirements of the CCO Annual Report; and (3) add the Registrant’s audit committee as a party that must receive the CCO Annual Report. The Commission believes that the proposed amendments will not impose any new information collection requirements that require approval of OMB under the PRA. As such, the proposed amendments do not impose any new burden or any new information collection

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<sup>50</sup> See Policy Statement and Establishment of Definitions of “Small Entities” for Purposes of the Regulatory Flexibility Act, 47 FR 18618, 18619 (Apr. 30, 1982) (FCMs); Further Definition of “Swap Dealer,” “Security-Based Swap Dealer,” “Major Swap Participant,” “Major Security-Based Swap Participant” and “Eligible Contract Participant,” 77 FR 30596, 30701 (May 23, 2012) (SDs and MSPs).

<sup>51</sup> 44 U.S.C. 3501 et seq.

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

As discussed above, the Commission is proposing amendments to the CCO Rules that would: (1) define the term "senior officer"; (2) provide greater specificity regarding the scope of the CCO's duties; (3) clarify the content requirements for the CCO Annual Report; and (4) require a Registrant's audit committee (or equivalent body), board of directors, and the senior officer to receive the CCO Annual Report. The baseline for this cost and benefit consideration is existing § 3.3.<sup>52</sup>

The proposed amendments to § 3.3(d) do not change the CCO duties, but rather provide greater specificity regarding the scope of the CCO's duties and further harmonize with the SEC's security-based swap dealer CCO duties. The Commission expects that greater clarity concerning CCO responsibilities will reduce the potential burdens on CCOs and improve the benefits of compliance by allowing CCOs to better focus on the fundamental compliance aspects of their responsibilities. Additionally, by further harmonizing the CFTC's and SEC's CCO duties, CCOs of dual registrants should be able to fulfill their duties more cost effectively.

Because the proposed amendments to § 3.3(d) do not expand the CCO duties, the Commission preliminarily believes that the proposal would not impose any additional costs to Registrants, market participants, the markets, or the general public. The Commission, however, invites comment regarding the nature of, and the extent to which,

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<sup>52</sup> The Commission notes that adding a definition of "senior officer" would be effected by amending § 3.1. The Commission believes this addition in and of itself has no impact for purposes of determining the costs and benefits of the proposal, and, therefore, is restricting its analysis of the costs and benefits to the proposed amendments to § 3.3. Nevertheless, the Commission is seeking public comment on whether the definition of "senior officer" has any cost and benefit considerations.

costs associated with the CCO duties described in § 3.3(d) could change as a result of the adoption of the proposal and, to the extent they can be quantified, monetary and other numerical estimates thereof.

As discussed more fully above, in implementing § 3.3(e) and (f), 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 with respect to time and resources. The proposed amendments to eliminate the requirement-by-requirement assessment are intended to reduce the cost to Registrants of producing the CCO Annual Report while maintaining its critical purpose. 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. In addition, the amendments would 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 foregoing amendments would also provide relief for Registrants from resource and time pressures in preparing their CCO Annual Reports.

The Commission recognizes that the CCO Annual Reports may contain less content if the proposed amendments are adopted because of the removal of the process of documenting a review for hundreds of individual regulatory requirements. However, many of the requirements are inter-related and are better addressed collectively.<sup>53</sup> In addition, eliminating this process should allow Registrants to focus more fully on

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<sup>53</sup> For example, under the current regulations 3.3(e) and (f), an assessment of §§ 23.400 through 23.451, 17 CFR 23.400 through 23.451, governing business conduct standards for swap dealers and major swap participants with counterparties would require a separate assessment of each rule, and in many cases, each subsection as a separate “requirement.” However, because these regulations all address external business conduct standards, it may be appropriate to address these rules together.

completing their internal review processes and encourage more focused discussion of material issues in the CCO Annual Report. While the proposed amendments may require less description and classification, the Commission believes that a more focused, substantive discussion of the Registrant's assessment and material compliance issues will result in a CCO Annual Report that is a more effective tool for informing both the Registrant's senior management and the Commission as to the status of compliance at the firm.

1. Section 15(a) Factors

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.<sup>54</sup> 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.

The Commission believes that the CCO Rules reinforce the CEA's protections for swap markets participants, futures market participants, and the public as more fully described in the CCO Rules Adopting Release.<sup>55</sup> This proposal does not seek to diminish either the role of the CCO or the value of the CCO Annual Report. On the contrary, the Commission believes that the proposal will provide the CCO with greater flexibility in accomplishing their duties and focusing compliance resources. Further, the proposal

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<sup>54</sup> 7 U.S.C. 19(a).

<sup>55</sup> See, e.g., CCO Rules Adopting Release, 77 FR at 20193.

should lead to a CCO Annual Report that more effectively and efficiently focuses the Registrant's board, senior management, and as proposed, the audit committee, as well as the Commission on areas requiring change or improvement.

a. Protection of Market Participants and the Public

The proposed amendments 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 reporting detail, the Commission believes that change will allow the CCO to focus on identifying and describing in the CCO Annual Report material compliance matters that deserve greater attention. Accordingly, the Commission preliminarily believes that the reduction in content requirements will not affect the protection of market participants and the public.

b. Efficiency, Competitiveness, and Financial Integrity of Markets

The Commission preliminarily believes that the proposed amendments to the CCO Rules could improve resource allocational efficiency for Registrants by reducing the burden to produce the CCO Annual Reports thereby allowing Registrants to allocate compliance resources used for report preparation more efficiently. Furthermore, entities that are dually registered with the CFTC and SEC and that must comply with the CCO Rules are likely to benefit from greater efficiencies to the extent the two agencies' parallel regulations are consistent. The Commission preliminarily believes that the proposed amendments to the CCO Rules will not have any negative impacts on market efficiency, competitiveness, or integrity because each CCO Annual Report addresses

internal compliance programs of each Registrant and are not publicly available, and the amendments affecting CCO duties only clarify those duties and do not affect markets.

c. Price Discovery

The Commission has not identified a specific effect on price discovery as a result of the proposal because the proposal does not address any pricing issues. Nevertheless, the Commission seeks public comment on this issue.

d. Sound Risk Management Practices

The Commission preliminarily believes that the proposed amendments to the CCO duties and CCO Annual Report requirements would not have a meaningful effect on the risk management practices of Registrants. The proposed amendments relating to the CCO's duties and annual report 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>56</sup> Furthermore, the proposed amendments to the 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. Finally, the Commission preliminarily believes that including the audit committee and both the board of directors and the senior officer as recipients of the CCO Annual Reports may benefit Registrants' overall risk management practices by ensuring that all groups with overall responsibility for governance and internal controls are informed of the report contents.

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<sup>56</sup> See, e.g., 17 CFR 23.600.

e. Other Public Interest Considerations

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

Request for Comment: The Commission invites comment on its preliminary consideration of the costs and benefits associated with the proposal, especially with respect to the five factors the Commission is required to consider under CEA section 15(a). In addressing these areas and any other aspect of the Commission's preliminary cost-benefit considerations, the Commission encourages commenters to submit any data or other information they may have quantifying and/or qualifying the costs and benefits of the proposal.

**List of Subjects in 17 CFR Part 3**

Registration.

For the reasons stated in the preamble, the Commodity Futures Trading Commission proposes to amend 17 CFR part 3 as set forth below:

**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, as amended by Title VII of Pub. L. 111-203, 124 Stat. 1376.

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)(1) to read as follows:

**§ 3.3 Chief compliance officer.**

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(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 any conflicts of interest 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, including through ensuring that the registrant establishes, maintains, and reviews written policies and procedures reasonably designed to achieve compliance;

(4) Establishing, maintaining, and reviewing 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) Establishing 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 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 to the Commission. (1) Prior to furnishing the annual report to the Commission, the chief compliance officer shall provide the annual report to the board of directors, the senior officer, and the audit committee (or equivalent body) of the futures commission merchant, swap dealer, or major swap participant for its review. Furnishing the annual report to the board of directors, the senior officer, and the audit committee (or equivalent body) shall be recorded in the board minutes or otherwise, as evidence of compliance with this requirement.

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Issued in Washington, DC, on May 3, 2017, by the Commission.

Christopher J. Kirkpatrick,  
Secretary of the Commission.

NOTE: The following appendix will not appear in the Code of Federal Regulations.

**Appendix to Chief Compliance Officer Duties and Annual Report Requirements for  
Futures Commission Merchants, Swap Dealers, and Major Swap Participants;  
Amendments – Commission Voting Summary**

On this matter, Acting Chairman Giancarlo and Commissioner Bowen voted in the affirmative. No Commissioner voted in the negative.

[FR Doc. 2017-09229 Filed: 5/5/2017 8:45 am; Publication Date: 5/8/2017]