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CITY BAR

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March 21, 2022

Vanessa A. Countryman  
Secretary  
U.S. Securities and Exchange Commission  
100 F Street, N.E.  
Washington, D.C. 20549-1090

**Re: Prohibition Against Fraud, Manipulation, or Deception in Connection with Security-Based Swaps; Prohibition against Undue Influence over Chief Compliance Officers; Position Reporting of Large Security-Based Swap Positions (Exchange Act Release No. 34-93784 (December 15, 2021)): File No. S7-32-10; RIN 3235-AK77**

Dear Ms. Countryman:

The New York City Bar Association's Compliance Committee (the "Compliance Committee") submits this letter in response to the request of the Securities and Exchange Commission (the "SEC" or the "Commission") for comment on Exchange Act Release No. 93784 (December 15, 2021), in which the Commission proposed rules as part of its broader efforts under the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank") to address misconduct in the security-based swap market, promote compliance with the federal securities laws by security-based swap dealers and major security-based swap participants ("SBS Entities"), and increase transparency in the security-based swap market (collectively, the "Proposal" or the "Proposing Release"). The Compliance Committee appreciates the opportunity to comment on the Commission's Proposal.

This comment letter focuses on the Chief Compliance Officer ("CCO") independence provisions proposed under new Rule 15Fh-4(c) (the "CCO Provision") and does not express any opinion on the rest of the Proposal. The Compliance Committee substantially supports the CCO Provision, but based on the diversity and experience of its membership, is offering comments to

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*The mission of the New York City Bar Association, which was founded in 1870 and has 25,000 members, is to equip and mobilize a diverse legal profession to practice with excellence, promote reform of the law, and uphold the rule of law and access to justice in support of a fair society and the public interest in our community, our nation, and throughout the world.*

assist the Commission in further evaluating the CCO Provision. The Compliance Committee membership includes many compliance professionals at various financial institutions, in addition to attorneys from law firms, in-house counsel, consultants, and representatives of regulatory and government agencies. We believe the Compliance Committee's diverse membership focused on the compliance function enables it to provide a thoughtful view on matters impacting the compliance function specifically and the financial community generally.

## **I. SUMMARY**

The Proposal seeks input on re-proposed new Rule 9j-1 under the Securities Exchange Act of 1934 (the "Exchange Act"), which would be designed to prevent fraud, manipulation, and deception in connection with all transactions in security-based swaps, including misconduct in connection with the exercise of any right or performance of any obligation under a security-based swap. The Proposal also seeks input on proposed new Rule 15Fh-4(c) under the Exchange Act, which would make it unlawful for any officer, director, supervised person, or employee of an SBS Entity, or any person acting under such person's direction, to directly or indirectly take any action to coerce, manipulate, mislead, or fraudulently influence the SBS Entity's CCO in the performance of his or her duties under the federal securities laws or the rules and regulations thereunder. Finally, the Proposal seeks input on proposed new Rule 10B-1 under the Exchange Act, which would require any person with a security-based swap position that exceeds a certain threshold to promptly file with the Commission a schedule disclosing certain information related to its position.

As we discuss further below, the Compliance Committee shares the Commission's view that CCOs of SBS Entities play a critical role in preventing fraud and manipulation by SBS Entities and their personnel through designing and maintaining effective compliance systems. The Compliance Committee supports the Commission's proposal to adopt an additional measure under Section 15F(h) of the Exchange Act to protect CCOs in the furtherance of those duties. In particular, we agree with the Commission that a rule expressly prohibiting interference with the performance of a CCO's duties is critical at all times, but all the more so now, given those duties are now more well developed and express. If adopted, we agree that the CCO Provision will help to deter attempts by officers, directors, supervised persons, or employees to hide transactions, submit false valuations, or otherwise manipulate or fraudulently influence a CCO in the performance of his or her duties.

In this comment letter, we first discuss the substantial obligations that CCOs of SBS Entities have and highlight the continuing perceived increased risk of personal liability of CCOs. We then highlight the Compliance Committee's agreement with the Commission that now is an opportune time to adopt the CCO Provision, and we discuss how adoption of the CCO Provision would bolster existing CCO reporting line requirements and CCO compensation and removal requirements that are intended to protect the integrity of the compliance functions in SBS Entities. Finally, we discuss the ample precedent that exists for adopting the CCO Provision.

## **II. CCOs OF SBS ENTITIES HAVE SUBSTANTIAL OBLIGATIONS AND ARE CRITICAL TO EFFECTIVE RISK MANAGEMENT**

The duties for which a CCO of an SBS Entity is responsible are both many and essential to establishing an effective risk management program at an SBS Entity. For example, among other

obligations, this includes (i) reporting directly to the board of directors or to the senior officer of the SBS Entity,<sup>1</sup> (ii) taking reasonable steps to ensure that the SBS Entity establishes, maintains, and reviews written policies and procedures reasonably designed to achieve compliance with the Exchange Act and the rules and regulations thereunder relating to its business as an SBS Entity,<sup>2</sup> (iii) taking reasonable steps, in consultation with the board of directors or the senior officer of the SBS Entity, to resolve any material conflicts of interest that may arise,<sup>3</sup> and (iv) administering each required policy and procedure.<sup>4</sup> Moreover, a CCO must annually prepare and sign a compliance report that describes the SBS Entity’s written policies and procedures (including code of ethics and conflict of interest policies), the effectiveness of such policies and procedures, any material changes to such policies and procedures, areas for improvement, any material non-compliance matters identified, and the financial, managerial, operational, and staffing resources set aside for compliance with requirements applicable to the SBS Entity.<sup>5</sup> Finally, CCOs have various duties in connection with rules that allow SBS Entities to manage market, counterparty, operational, and legal risks associated with their businesses, including related to trading relationship documentation, dispute resolution, portfolio reconciliation, and portfolio compression (“Risk Mitigation Rules”), as well as rules relating to capital, margin, and segregation requirements and recordkeeping and reporting.<sup>6</sup>

Despite these duties, there is a structural tension inherent in the role of compliance officers given that they are employees whose jobs and livelihoods ultimately depend on their employers. Accordingly, it is imperative that market participants have CCOs with real authority and autonomy to influence corporate decision-making to prevent or head off risks and to police firms from within. Indeed, this is one of the most efficient and effective tools available to regulators. In the performance of their duties, CCOs prevent numerous violations of the securities laws, and regulators would be stretched far too thin if their capabilities were not supplemented in this way. This is all the more important today, as CCOs continue to face a perceived increased risk of individual liability, which flows from an increase in enforcement actions brought against

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<sup>1</sup> See 17 C.F.R. § 240.15Fk-1(b)(1).

<sup>2</sup> See *id.* § 240.15Fk-1(b)(2). This includes (i) reviewing the compliance of the SBS Entity with requirements described in Exchange Act Section 15F, and the rules and regulations thereunder, including preparing the entity’s annual assessment of its written policies and procedures, (ii) taking reasonable steps to ensure that the entity establishes, maintains, and reviews policies and procedures reasonably designed to remediate non-compliance issues identified by the CCO, whether through office reviews, look-backs, audit findings, self-reporting, or validated complaints, and (iii) taking reasonable steps to ensure that the entity establishes and follows procedures reasonably designed for the handling, management response, remediation, retesting, and resolution of non-compliance issues.

<sup>3</sup> See *id.* § 240.15Fk-1(b)(3).

<sup>4</sup> See *id.* § 240.15Fk-1(b)(4).

<sup>5</sup> See *id.* § 240.15Fk-1(c).

<sup>6</sup> See Risk Mitigation Techniques for Uncleared Security-Based Swaps, Exchange Act Release No. 87762 (Dec. 18, 2019), 85 Fed. Reg. 6359 (Feb. 4, 2020) (“Risk Mitigation Rules Adopting Release”). See also Capital, Margin, and Segregation Requirements for Security-Based Swap Dealers and Major Security-Based Swap Participants and Capital and Segregation Requirements for Broker-Dealers, Exchange Act Release No. 86175 (June 21, 2019), 84 Fed. Reg. 43872 (Aug. 22, 2019) (“Capital, Margin, and Segregation Adopting Release”); Recordkeeping and Reporting Requirements for Security-Based Swap Dealers, Major Security-Based Swap Participants, and Broker-Dealers, Exchange Act Release No. 87005 (Sept. 19, 2019), 84 Fed. Reg. 68550 (Dec. 16, 2019) (“Recordkeeping and Reporting Adopting Release”).

compliance officers, recent regulatory focus on holding individuals liable for compliance failures,<sup>7</sup> and an expanding set of regulatory requirements that stretch the compliance function’s resources and present greater exposure for compliance officers in their individual capacity.<sup>8</sup>

In a number of regulatory actions, CCOs appear to be held personally liable by regulators for having “caused” their firms’ failures to design and implement effective policies and procedures. CCOs may sometimes be singled out as the individual responsible for an entity’s failure to adopt and follow compliance policies and procedures even though, by statute, these responsibilities fall on the regulated entity rather than any particular employee.<sup>9</sup> There are various obligations under the Exchange Act for SBS Entities, however, that are expressly imposed on CCOs.

Empowering CCOs, and the compliance function writ large, with real authority and independence can offer CCOs comfort that (i) they can provide objective advice and counsel that will be appropriately considered and (ii) a culture of compliance can be achieved at their firms with less risk of inappropriate retribution. This should reduce the risk of individual CCO liability and, as importantly, also promote security-based swap businesses in which the pursuit of profits is appropriately balanced by compliance with applicable law. Taking steps to protect CCOs’ independence in their fulfillment of their various duties, such as by adopting the CCO Provision, is an entirely appropriate endeavor by the Commission.

### **III. THE TIME IS RIPE TO ADOPT A RULE PREVENTING UNDUE INFLUENCE ON CCOs**

The Compliance Committee agrees with the Commission that now is an opportune time to adopt the CCO Provision. The Commission previously considered whether to adopt a rule on

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<sup>7</sup> See Andrew Ceresney, Dir., Div. of Enf’t, U.S. Sec. & Exch. Comm’n, Keynote Address at Compliance Week 2014 (May 20, 2014) (noting that the SEC has brought “and will continue to bring – actions against legal and compliance officers”).

<sup>8</sup> The long-term increase in the risk of individual liability is well documented. As just one example, in its 2005 *White Paper on the Role of Compliance*, the Securities Industry Association (now the Securities Industry and Financial Markets Association (“SIFMA”)) noted that “[o]nly in limited circumstances have the [SEC] and [self-regulatory organizations] brought failure to supervise actions against non-line personnel, such as Compliance Department officers.” *White Paper on the Role of Compliance*, THE SEC. INDUS. ASS’N 11 (Oct. 2005), <https://www.sifma.org/wp-content/uploads/2017/08/2005RoleofComplianceWhitePaper.pdf> (last visited Mar. 9, 2022). By 2013, SIFMA noted, in *The Evolving Role of Compliance*, that “the view of enforcement authorities of Compliance’s role” had “recently” changed, as compliance personnel had been named in enforcement actions advancing then-novel theories under which compliance personnel could be held liable for failures to “supervise” others who engaged in alleged violations. See *The Evolving Role of Compliance*, THE SEC. INDUS. AND FIN. MARKETS ASS’N 9 (Mar. 2013), <https://www.sifma.org/wp-content/uploads/2017/05/the-evolving-role-of-compliance.pdf> (last visited Mar. 9, 2022).

<sup>9</sup> See, e.g., Investment Advisers Act Release No. 4065 (Aug. 6, 2015), <https://www.sec.gov/litigation/admin/2015/ia-4065.pdf> (last visited Mar. 9, 2022) (the SEC charged BlackRock Advisors’ CCO with having “caused” BlackRock to willfully violate rules under the Advisers Act and certain BlackRock funds to violate the Investment Company Act even though the statutes and rules impose requirements on the investment adviser generally, not specifically on an adviser’s CCO); Windsor Street Capital, L.P., Exchange Act Release No. 80908 (June 12, 2017), <https://www.sec.gov/litigation/admin/2017/34-80908.pdf> (last visited Mar. 9, 2022) (finding the CCO liable for aiding and abetting and causing the firm’s failure to file suspicious activity reports under the Bank Secrecy Act despite such requirements applying solely to the firm).

undue influence over CCOs in 2016 when it adopted business conduct standards for SBS Entities.<sup>10</sup> At the time, however, the Commission had not finalized most of the requirements for which the CCO of an SBS Entity would be responsible. The Commission has now finalized a majority of its Dodd-Frank Title VII rules related to security-based swaps and SBS Entities,<sup>11</sup> and, as discussed above, the duties for which a CCO is now responsible are both many and essential to establishing an effective risk management program at an SBS Entity. The CCO Provision, if adopted, would help ensure that CCOs have the independence to effectively fulfill their duties to the SBS Entities and that their fulfillment of those duties is not inappropriately colored by the interests or misconduct of others associated with the SBS Entity.

#### **IV. RULE 15Fh-4(c) WOULD REINFORCE EXISTING CCO INDEPENDENCE REQUIREMENTS**

The Compliance Committee applauds the Commission for its prior adoption of the business conduct standards, in particular its adoption of the Reporting Line and Compensation and Removal requirements.<sup>12</sup> However, the Compliance Committee believes that these requirements may not be sufficient to protect the independence and objectivity of an SBS Entity CCO. This is particularly the case given the expanded duties now expressly imposed on such CCOs that touch on diverse and complex aspects of an SBS Entity's business. The Compliance Committee strongly believes that the Commission should adopt measures to expand the protections afforded CCOs of SBS Entities and prohibit interference with the performance of a CCO's duties, even if not directly related to compensation or the threat of removal of the CCO.

While the Reporting Line and Compensation and Removal requirements were welcome additions to protect the integrity of the compliance functions in SBS Entities, they focus on establishing structures to mitigate possible conflicts of interest that could interfere with a CCO's independent advice and counsel, and particularly with respect to those to whom a CCO may report. They do not, however, make explicit that no personnel of an SBS Entity – whether an officer, director, or any other supervised person or employee – may seek to unduly influence the execution of the CCO's role.

The CCO Provision, if adopted, would essentially address conflicts and possible “bad acts” by persons above, below, and at the same level of the CCO, including persons directed by any such persons, thereby ensuring that the entire continuum of personnel at an SBS Entity is subject to a prohibition against seeking to unduly influence the CCO. The duties of a CCO span many areas of an SBS Entity's business and require input from all levels of seniority in the organization. If an

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<sup>10</sup> See Business Conduct Standards for Security-Based Swap Dealers and Major Security-Based Swap Participants, Release No. 77617 (Apr. 14, 2016), 81 Fed. Reg. 29960 (May 13, 2016) (“Business Conduct Standards Adopting Release”). The adopted business conduct standards include, among other obligations, (i) Rule 15Fk-1(a) and (b), which respectively require that an SBS Entity designate a CCO and impose certain duties and responsibilities on that CCO, (ii) Rule 15Fk-1(b)(1), which requires that an SBS Entity CCO report directly to the board of directors or to the senior officer of the SBS Entity (the “Reporting Line” requirement), and (iii) Rule 15Fk-1(d), which requires that the compensation and removal of the CCO be approved by a majority of the board of directors of the SBS Entity (the “Compensation and Removal” requirement).

<sup>11</sup> See Risk Mitigation Rules Adopting Release, *supra* note 6. See also Capital, Margin, and Segregation Adopting Release, *supra* note 6; Recordkeeping and Reporting Adopting Release, *supra* note 6.

<sup>12</sup> See Business Conduct Standards Adopting Release, *supra* note 10 (describing adoption of the business conduct standards, including the Reporting Line requirement and Compensation and Removal requirement).

individual associated with an SBS Entity intends to participate in the triggering of manufactured credit events or in other opportunistic strategies, whether through submitting false valuations, creating artificial events to trigger security-based swap obligations, or otherwise attempting to manipulate security-based swap obligations, such activities can originate at any level in the organization. It is not clear that the current Reporting Line and Compensation and Removal requirements would in any way prevent or mitigate the likelihood that such activities would occur.

Given that attempts by officers, directors, supervised persons, or employees to hide transactions, submit false valuations, or manipulate or fraudulently influence a CCO in the performance of his or her duties, including related to the Risk Mitigation Rules, would undermine an SBS Entity's risk management and thus could pose risk to the market, the Compliance Committee agrees that it is appropriate to adopt a rule expressly prohibiting interference with the performance of a CCO's duties, particularly now that those duties are now more well developed and express.

#### V. PRECEDENT SUPPORTS ADOPTION OF RULE 15Fh-4(c)

There is ample precedent supporting the Commission's adoption of the CCO Provision that has been widely accepted by the industry. For example:

- **Exchange Act Rule 13b2-2** – In 2003, pursuant to Section 303(a) of the Sarbanes-Oxley Act of 2002, the Commission adopted rules supplementing Regulation 13B-2, which addresses the falsification of books, records, and accounts and false or misleading statements, or omissions to make certain statements, to accountants.<sup>13</sup> Specifically, the SEC adopted Rule 13b2-2(b)(1), which prohibits officers and directors, and persons acting under their direction, from coercing, manipulating, misleading, or fraudulently influencing the auditor of an issuer's financial statements when the officer, director, or other person knew or should have known that the action, if successful, could result in rendering the issuer's financial statements materially misleading.<sup>14</sup> The SEC also adopted Rule 13b2-2(b)(2) to provide examples of actions that improperly influence an auditor that could result in rendering the issuer's financial statements materially misleading, as well as Rule 13b2-2(c), which applies similar provisions to audits of investment companies' financial statements.<sup>15</sup>

- **Exchange Act Rule 13n-11** – In 2015, the SEC adopted Rule 13n-11(h) in relation to security-based swap data repositories ("SDRs").<sup>16</sup> That rule states that "[n]o officer, director, or employee of a security-based swap data repository may directly or indirectly take any action to coerce, manipulate, mislead, or fraudulently influence the security-based swap data repository's chief compliance officer in the performance of his or her duties under this section."<sup>17</sup> Like the

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<sup>13</sup> See *Improper Influence on Conduct of Audits*, Exchange Act Release No. 47890 (May 20, 2003), 68 Fed. Reg. 31820 (May 28, 2003).

<sup>14</sup> See 17 C.F.R. § 240.13b2-2(b)(1).

<sup>15</sup> See *id.* at § 240.13b2-2(b)(2) & (c).

<sup>16</sup> *Security-Based Swap Data Repository Registration, Duties, and Core Principles*, Exchange Act Release No. 74246 (Feb. 11, 2015), 80 Fed. Reg. 14438 (Mar. 19, 2015).

<sup>17</sup> 17 C.F.R. § 240.13n-11(h).

CCO Provision, Rule 13n-11(h) was designed to prevent personnel at an SDR from seeking to improperly affect the SDR's CCO in the performance of his or her responsibilities and more generally to promote the independence of an SDR's CCO while maintaining the CCO's effectiveness by mitigating the potential conflicts of interest between the CCO and the SDR's officers, directors, and employees.

- **Investment Company Act Rule 38a-1** – In 2003, the SEC adopted Rule 38a-1 under the Investment Company Act of 1940, which requires fund boards to adopt written policies and procedures reasonably designed to prevent the fund from violating the federal securities laws.<sup>18</sup> The procedures must provide for the oversight of compliance by the fund's advisers, principal underwriters, administrators, and transfer agents through which the fund conducts its activities. Rule 38a-1(a)(4) includes a requirement that each fund designate one CCO responsible for administering the fund's policies and procedures whose designation and compensation must be approved by the fund's board of directors, including a majority of the directors who are not interested persons of the fund.<sup>19</sup> Rule 38a-1(c) prohibits undue influence and states:

No officer, director, or employee of the fund, its investment adviser, or principal underwriter, or any person acting under such person's direction may directly or indirectly take any action to coerce, manipulate, mislead, or fraudulently influence the fund's chief compliance officer in the performance of his or her duties under this section.<sup>20</sup>

Like accountants, CCOs of SDRs, and fund CCOs, CCOs for SBS Entities are critical gatekeepers to the financial markets. This is especially the case given the size and importance of the security-based swap market to the financial markets more broadly and given that the security-based swap market is highly concentrated among a fairly small number of dealers. The Compliance Committee believes that the Commission should adopt the CCO Provision as proposed because further strengthening the objectivity and independence of SBS Entities' CCOs – key gatekeepers to the security-based swap market – is directly aligned with other well-established regulatory objectives, as noted above, as well as the broader objectives of Dodd-Frank Title VII.

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The Compliance Committee appreciates the opportunity to comment on the Proposal and applauds the comprehensive effort of the Commission and its staff to continue efforts to finalize

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<sup>18</sup> Compliance Programs of Investment Companies and Investment Advisers, Investment Advisers Act Release No. 2204 (Dec. 17, 2003), 68 Fed. Reg. 74714 (Dec. 24, 2003).

<sup>19</sup> See 17 C.F.R. § 270.38a-1(a)(4).

<sup>20</sup> *Id.* § 270.38a-1(c).

its Dodd-Frank regime for security-based swaps, including its proposed rules to address misconduct in the security-based swap market. If we can be of any further assistance in this regard, please feel free to contact us.

Respectfully submitted,



Patrick T. Campbell  
Chair, Compliance Committee

cc: The Hon. Gary Gensler, Chairman  
The Hon. Hester M. Peirce, Commissioner  
The Hon. Allison Herren Lee, Commissioner  
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