National Society of Compliance Professionals ("NSCP")
Firm and CCO Liability Framework

To help ensure investor protection and market integrity through effective compliance functions at broker-dealers, investment advisers and investment companies (together, "firm" and "firms"), the NSCP proposes a *Firm and CCO Liability Framework* (the "NSCP Framework") to provide guidance to regulators, chief compliance officers (CCOs), and firms regarding perceived or actual CCO liability. As the premier financial industry organization that educates and advocates on behalf of compliance professionals, the NSCP is uniquely positioned to examine the practical challenges faced by CCOs as part of the larger governance structure at firms, and provide context that goes beyond the technical aspects of compliance as it relates to CCO liability.

Background: To highlight these challenges, the NSCP conducted multiple industry-wide surveys focusing on "CCO Liability" and "CCO Empowerment" with its 2000+ membership of CCOs and other compliance professionals. The results of the surveys demonstrated compliance professionals remain concerned that personal liability will be imposed in cases where:

- Compliance acted negligently rather than recklessly (53%);
- Compliance relied on inaccurate data from another employee (66%); and
- Compliance did not participate in the violations caused by the company or other executives (63%).[1]

In addition, 72% of compliance professionals are concerned that regulators have expanded the role of compliance officers and the scope of their responsibilities in imposing personal liability; 70% believe the overall compliance function at their firms is under resourced; 35% reported insufficient resources to conduct compliance training; 20% reported insufficient authority to develop and enforce compliance policies and procedures at their firms; and 25% reported an inability to address compliance-related weaknesses and report concerns to senior management.

Imposing personal liability on CCOs who have not engaged in misconduct or obstruction has the impact of shifting responsibility from business line personnel and management to the CCO. This could diminish the culture of compliance within firms and promote indifference from business line employees and management to follow the rules. It could ultimately lead to firm-wide deficiencies being attributed to compliance and benefit management who failed to empower compliance. While securities regulators have expressed support for CCO empowerment and the enhancement of compliance resources,[2] NSCP's surveys demonstrate that significant practical concerns still exist. Many compliance departments continue to be viewed as cost centers, not receiving the proper support, resources, or authority from their firm to appropriately address compliance-related weaknesses.

To more effectively address the issue of CCO liability, the NSCP believes it is necessary to focus on the larger context of the compliance function within firms and to do so earlier in regulatory reviews, whether during examinations or enforcement investigations. While the NSCP supports the New York City Bar's "Framework for Chief Compliance Officer Liability in the Financial Sector" and the recklessness standard it articulates,[3] the NSCP believes that a framework focused on evaluating CCO liability based solely on of the responsibilities and expectations of the position is only a partial solution. Careful consideration must be given to the full context in which the CCO functioned. As a result, the NSCP is advocating an additional framework.

By bringing these concerns to the forefront, the NSCP hopes to alleviate the uncertainty faced by compliance officers and provide a framework that more directly aligns with statements made by SEC and FINRA

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[1] NSCP CCO Liability Survey and NSCP CCO Empowerment and Resources Survey

[2] *See, e.g.,* SEC.gov | The Role of the CCO – Empowered, Senior and With Authority (https://www.sec.gov/news/speech/driscoll-role-cco-2020-11-19)

[3] NYC Bar CCO Liability Report (https://s3.amazonaws.com/documents.nycbar.org/files/NYC_Bar_CCO_Framework.pdf)

leadership and industry professionals, and promotes investor protection and market integrity, as set forth below:

- ***Firms***: Firms of all sizes and structures should empower their CCOs with the full responsibility, ability and authority to develop, implement, and enforce appropriate policies and procedures. In addition, firm leadership needs to continually assess whether the compliance program has adequate resources to support a robust compliance function.[4]
- ***CCOs***: CCOs should have clear direction and agreement from firm leadership on their roles and authority to manage compliance programs specifically tailored to their firms and reasonably designed to prevent violations of federal securities laws.[5]
- ***Regulators***: Regulatory examination and enforcement teams should have an appropriate foundation to evaluate compliance failures identified during the course of examinations or investigations, and in particular, whether those failures rise to the level where formal charges should be referred to enforcement or brought against the CCO.

We hope the NSCP Framework serves as a useful tool for securities regulators moving forward and a springboard to continue the conversation on this important issue.

NSCP Framework: To evaluate the issue of CCO liability, the following questions should be considered by regulators where a compliance failure may have occurred. A "yes" answer to any of the questions below mitigates against CCO liability:

- Did the CCO have nominal rather than actual responsibility, ability, or authority to affect the violative conduct?
- Was there insufficient support from firm leadership to compliance, including, for example, insufficient resources, for the CCO to affect the violative conduct?
- Did the CCO escalate the issue or violative conduct to firm management through a risk assessment, annual review, CEO certification meeting/report, or otherwise?
- Did firm management fail to respond appropriately after becoming aware of the issue (through the CCO or otherwise)?
- If the firm made misstatements or omitted material information, did the CCO have nominal rather than actual responsibility, ability, or authority for reviewing or verifying that information?
- Was firm leadership provided the opportunity to review and accept the policies and procedures?
- Did the CCO consult with legal counsel (in-house or external) and/or securities compliance consultants and adhere to the advice provided?
- Did the CCO otherwise act to prevent, mitigate, and/or address the issue?
- Did the CCO reasonably rely on information from others in the firm or firm systems?

The NSCP believes the responses to these questions will help provide examination and enforcement teams with a framework through which to properly evaluate CCO liability.[6]

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[4] *See, e.g.*, SEC.gov | The Role of the CCO – Empowered, Senior and With Authority (https://www.sec.gov/news/speech/driscoll-role-cco-2020-11-19).
[5] *Id.*
[6] Please note, the NSCP Framework is not intended to focus on circumstances where the CCO otherwise acted inappropriately. *See* https://www.sec.gov/news/speech/keynote-address-2015-national-society-compliance-prof-cereseney.html (citing instances where (1) compliance personnel possessed supervisory responsibilities within a Firm's supervisory system and demonstrated a wholesale failure to discharge those responsibilities that were clearly assigned to them; (2) compliance personal affirmatively participated in misconduct; or (3) compliance personnel intentionally helped to mislead regulators).