



## U.S. COMMODITY FUTURES TRADING COMMISSION

Three Lafayette Centre  
1155 21st Street, NW, Washington, DC 20581  
Telephone: (202) 418-5000  
Facsimile: (202) 418-5521  
[www.cftc.gov](http://www.cftc.gov)

### Division of Swap Dealer and Intermediary Oversight

Matthew Kulkin  
Director

CFTC Letter No. 18-28  
Exemption  
December 4, 2018  
Division of Swap Dealer and Intermediary Oversight

Re: Exemption Pursuant to Commission Regulation 1.16(f)(2) for Audit Standards Requirements for FCM Certified Financial Statements for Year Ending December 31, 2018

Dear :

This is in response to your letter dated October 15, 2018, to the Division of Swap Dealer and Intermediary Oversight (“the Division” or “DSIO”) of the Commodity Futures Trading Commission<sup>1</sup> (“Commission”). By your letter, you request on behalf of [“A”], a registered futures commission merchant (“FCM”), that the Division exempt, pursuant to Commission Regulation 1.16(f)(2),<sup>2</sup> A from Regulation 1.16(c)(2) with respect to its compliance with certain auditor independence standards adopted by the Public Company Accounting Oversight Board (“PCAOB”) for the examination of A’s annual financial statement.

#### I. Regulatory Background

Commission Regulation 1.16 addresses the minimum requirements a public accountant must meet in order to be recognized by the Commission as qualified to conduct an examination for the purpose of expressing an opinion on the financial statements of an FCM. Prior to 2014, the Commission required that an FCM’s qualified independent accountant be duly registered and in good standing under the laws of their principal residence and that the accountant’s report state whether its audit was conducted in accordance with generally accepted auditing standards issued by the American Institute of Certified Public Accountants (“AICPA”). In 2013, the Commission amended Regulation 1.16 to require an FCM’s independent accountant to be both registered with the PCAOB and state whether its audit was performed in accordance with PCAOB auditing

---

<sup>1</sup> Commission regulations referred to in this letter are found at 17 C.F.R. Ch. I (2017). The Commission’s website, [www.cftc.gov](http://www.cftc.gov), provides links to the Regulations.

<sup>2</sup> Regulation 1.16(f)(2) provides, in relevant part, that the Commission may grant a conditional or unconditional exemption from any of the certified financial reporting requirements. The Commission has delegated the authority to grant the exemption to the Director of DSIO pursuant to Regulation 140.91.

standards.<sup>3</sup> In adopting these amendments, the Commission noted the unique role of FCMs in holding customer funds deposited to guarantee customer's positions in futures and cleared swaps and the desire to keep these requirements consistent with the requirements for auditors of broker dealers established by the Securities and Exchange Commission ("SEC").<sup>4</sup>

## II. Relief Requested

As represented in your letter, and from additional conversations, we understand the relevant facts to be as follows. ["B"], the parent entity and 100 percent owner of A, was acquired by an investment fund during October 2018. The investment fund is one of several investment funds under the ownership and control of a single legal entity.

["C"] is A's auditor. C has previously certified financial statements for A, and is currently engaged to provide the examination of A's financial statements for the year ending December 31, 2018.

You represent that the acquisition of B and A by the investment fund, has resulted in A having several thousand new affiliated entities as of December 31, 2018. You also represent that the addition of these new affiliates complicates and, in certain cases, may impair the independence analysis performed by C under auditing standards issued by the PCAOB. You further represent that A has incurred fees from C for work performed for the December 31, 2018 audit, and that additional costs would be incurred if A were required to terminate its relationship with C and engage a new audit firm that was unfamiliar with A's operations. Accordingly, you have requested that the Division exempt A from the PCAOB auditor independence standards, as required by Regulation 1.16(c)(2), with respect to A's financial statement examination.

In support of your request, you indicate that PCAOB and SEC auditor independence standards require an auditor to be independent from the audit client, which includes all affiliates of that audit client.<sup>5</sup> Those standards, disallow the provision of certain enumerated non-financial services to the audit client and its affiliates. You note that the PCAOB audit standards for independence cover an investment fund that owns a portfolio audit client, as well as any entities that control the fund, and all other entities, including funds, under common control with the investment fund. In A's case, you posit that this will result in 3,000-4,000 affiliates across multiple fund structures that will require an independence analysis.

In at least one case that has been identified, you state that C likely will be disqualified under PCAOB independence standards by the provision of one technology related non-financial services contract to a third-party because such contract is handled by a wholly-owned subsidiary

---

<sup>3</sup> See, *Enhancing Protections Afforded Customers and Customer Funds Held By Futures Commission Merchants and Derivatives Clearing Organizations*, 78 FR 68506 (Nov. 14, 2013); 17 C.F.R. 1.16(b)(1), (c)(2).

<sup>4</sup> *Id.* at 68526-68529.

<sup>5</sup> See, the definition of "affiliate" in both PCAOB Rule 3501 (a)(ii) and SEC Rule 2-01(f).

of a different investment fund within the same fund group which ultimately owns A. You state this other investment fund's subsidiary is a subcontractor on this non-financial services contract with a different international office of C. Nonetheless, the presence of such a relationship impairs independence under the SEC and PCAOB formulation of auditor independence, despite the lack of materiality of this contract to C's international office or any other connection of this other subsidiary and its other parent fund to A. As noted above, you further state that establishing auditor independence under the SEC and PCAOB formulation with respect to all such affiliates may require A to change auditors after the audit engagement period has begun, and this would create significant financial burden and hardship on A.

You note that the auditor independence standards of the AICPA do not require the same analysis regarding all affiliates as do PCAOB standards. Specifically, you state that AICPA auditor independence standards include an analysis of whether A is material to the acquiring entity before imputing all potential conflicts arising from the affiliates of the acquiring entity to A. You represent that in A's case, A is unlikely to be material to the acquiring investment fund at year-end, and the non-financial services contract is also not material to C. Further, there is no other relationship between A and the other wholly-owned subsidiary. Accordingly, you represent that C is able to satisfy the auditor independence standards required under AICPA generally accepted auditing standards. You further represent that, in addition to the immaterial nature of the non-financial services contract to C, the concerns of using AICPA independence standards is further mitigated by the fact that (i) the non-financial services contract involves an international office of C separate from the office that performs the audit of A and (ii) the other entity is wholly-owned by an investment fund that is separate from the investment fund that owns A. You further note that A is a retail forex dealer and does not carry futures or cleared swap customer accounts, and is not a clearing member of a derivatives clearing organization.

### III. Relief Granted

All Commission registrants required to file certified financial statements, other than FCMs, must have their auditor's report state whether the audit was done in accordance with AICPA standards.<sup>6</sup> As DSIO staff has previously stated, the Commission maintains its own auditor independence requirements under Regulation 1.16(b)(2), notwithstanding the separate independence requirements under auditing standards applicable to different registrants.<sup>7</sup> The Commission's independence formulation does not apply a materiality threshold to the

---

<sup>6</sup> See 17 C.F.R. 1.16 (a)(2).

<sup>7</sup> See 17 C.F.R. 1.16(b)(2); *Interpretation of Commission Regulation 1.16 Auditor Independence Standards for Audits of Futures Commission Merchants*, CFTC Letter No. 14-40 (March 28, 2014), stating the Division's belief that an FCM's auditor could demonstrate compliance with Regulation 1.16 by complying with SEC Rule 17a-5, which includes a reference to the independent requirements in SEC Rule 2-01 of Regulation S-X. In that letter, DSIO also stated its belief that certain PCAOB requirements, which were only applicable to issuers and not to broker-dealers, were not required for FCM auditors in order to maintain compliance with Regulation 1.16. Further, DSIO did not state that the SEC/PCAOB independence formulation was necessary to comply with Regulation 1.16, only that if followed it would satisfy Regulation 1.16.

assessment of affiliates or conflicts. Further, the Commission's independence formulation in Regulation 1.16(b)(2) disallows direct or material indirect financial interest and the provision of financial and accounting services to both the registrant and affiliate, but unlike the PCAOB/SEC standard, does not prohibit the provision of non-financial services to either. The Commission's auditor independence requirement is an "independence in fact" standard, and as such, any independence determination involves an examination of the facts and circumstances of the particular auditor's engagement with the registrant.

C has been A's auditor for several years and does not provide any financial or accounting services to A or have any financial interest in A. The A affiliate associated with the non-financial services to a separate office of C is remote to A, and the non-financial services being provided are immaterial to C. As previously stated, the provision of non-financial services to an affiliate of A does not impair independence under the Commission's regulation unless such services actually impaired the professional judgment of C with respect to the audit of A, which DSIO staff has no indication is at issue in this circumstance. Engaging a new auditor would be costly and could involve additional delays or operational burdens to both A and C. DSIO staff notes that the Commission's own auditor independence requirement under Regulation 1.16 will continue to apply in addition to the AICPA audit standards which are applicable to other Commission registrants.

Therefore, in light of the representations made in your letter, the Division believes that granting A an exemption from Regulation 1.16(c)(2) with respect to the PCAOB auditor independence requirements for the year ending December 31, 2018 is neither contrary to the purposes of Regulation 1.16 nor the public interest. Accordingly, pursuant to Regulation 1.16(f)(2), as delegated to the Division by Regulation 140.91(a)(5), A is hereby granted an exemption from the requirements under Regulations 1.16(c)(2) that the certified financial statements for the year ended December 31, 2018 be audited in accordance with PCAOB audit independence standards. The exemption provided by the Division is subject to the following conditions:

1. A (and by extension, C) continues to be subject to the Commission's specific auditor independence requirements set forth in Regulation 1.16(b)(2) for the December 31, 2018 examination.
2. A (and by extension, C) is subject to the auditor independence standards established by the AICPA for the December 31, 2018 examination.

This letter and the exemption granted herein, is based on the representations that have been made to the Division. Any different, changed or omitted facts or conditions might render the exemption void. The exemption granted by this letter does not excuse persons relying on it from compliance with any other applicable requirements contained in the Commodity Exchange Act or in Commission regulations issued thereunder. If you have any questions regarding this letter, please contact Jennifer C.P. Bauer, Special Counsel, at (202) 418-5472.

Very truly yours,

Matthew Kulkin  
Director  
Division of Swap Dealer and  
Intermediary Oversight

Cc: Regina Thoele (via email)  
Senior Vice President, Compliance  
National Futures Association