

public arbitrators during the panel selection process, and minimize the burden of vetting additional public arbitrators later in the process.

FINRA is also proposing to amend Rule 12403(c)(2) to increase the number of strikes to the public arbitrator list from four to six, so that the proportion of strikes is the same under the amended rule as it is under the current rule. Task Force members felt strongly that parties wanted additional public arbitrators to choose from because they did not want FINRA to appoint lower ranked arbitrators to the panel. We are proposing to increase the number of strikes the parties can make to the newly increased public list to improve the likelihood that FINRA will appoint the parties' preferred arbitrators to the panel.

## 2. Statutory Basis

FINRA believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,<sup>6</sup> which requires, among other things, that FINRA rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. FINRA believes the proposed rule change would protect investors and the public interest by providing greater choice during the panel selection process for the parties in all customer cases with three arbitrators.

### *B. Self-Regulatory Organization's Statement on Burden on Competition*

FINRA does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. Current rules permit parties to an arbitration to strike a specified number of arbitrators from each list of arbitrators that FINRA sends them and require them to rank order the remaining arbitrators. The propensity to strike all non-public arbitrators combined with the current rules for selecting the panel has led to concerns that panels may include a party's least preferred arbitrator, thereby diminishing a party's overall satisfaction with the arbitration process at the forum.

To remedy this concern, FINRA proposes to expand the number of arbitrators on the public arbitrator list. The longer list will increase the parties' choice of arbitrators during the panel selection process, and will improve the likelihood that FINRA will appoint the parties' preferred arbitrators to the panel.

Forum users are likely to incur costs in vetting the five additional public arbitrators on the list FINRA would send them. However, forum practitioners have indicated that they would willingly incur the additional expense in order to have greater choice in selecting arbitrators.

### *C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others*

Written comments were neither solicited nor received.

## III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the **Federal Register** or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) By order approve or disapprove such proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

## IV. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

### *Electronic Comments*

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-FINRA-2016-022 on the subject line.

### *Paper Comments*

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549-1090. All submissions should refer to File Number SR-FINRA-2016-022. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements

with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for Web site viewing and printing in the Commission's Public Reference Room, 100 F Street NE., Washington, DC 20549-1090, on official business days between the hours of 10 a.m. and 3 p.m. Copies of such filing also will be available for inspection and copying at the principal office of FINRA. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-FINRA-2016-022 and should be submitted on or before August 5, 2016.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>7</sup>

**Robert W. Errett,**  
*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-78277; File No. SR-OCC-2016-007]

### Self-Regulatory Organizations; The Options Clearing Corporation; Order Approving Proposed Rule Change Related to The Options Clearing Corporation's Membership Approval Process

July 11, 2016.

On May 16, 2016, The Options Clearing Corporation ("OCC") filed with the Securities and Exchange Commission ("Commission") the proposed rule change SR-OCC-2016-007 pursuant to Section 19(b)(1) of the Securities and Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4 thereunder.<sup>2</sup> The Commission did not receive any comments on the proposed rule change. This order approves the proposed rule change.

#### I. Description

OCC is changing its rules to: (i) Vest the authority to approve or disapprove

<sup>7</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>6</sup> 15 U.S.C. 78o-3(b)(6).

new membership applications with OCC's Risk Committee,<sup>3</sup> and (ii) delegate authority to the Executive Chairman or President of OCC to approve new membership applications provided that: (a) It is not recommended that the Risk Committee impose additional membership criteria upon the applicant pursuant to Section 1, Interpretation and Policy .06 of Article V of OCC's By-Laws, and (b) the Risk Committee is given not less than five business days to determine that the application should be reviewed at a meeting of the Risk Committee and the Risk Committee has not requested that the application be reviewed at a meeting of the Risk Committee within such five day period.

This proposed rule change will streamline OCC's membership approval process by: (i) Allowing OCC's Executive Chairman or President to approve pro forma applications for clearing membership, and (ii) vesting ultimate authority with OCC's Risk Committee, not its Board, to approve or disapprove applications for clearing membership that are not approved by either OCC's Executive Chairman or President. The practical effect of the proposed rule change is that either OCC's Executive Chairman or President will approve most applications for clearing membership at OCC since most applicants for clearing membership choose to have their application presented for approval only when such approval is pro forma in nature (*i.e.*, the applicant meets all of the clearing membership requirements at OCC and there is no need to impose additional membership requirements). OCC believes that the proposed rule change will better allocate the time and resources of the Board and Risk Committee and ensure applications for clearing membership are considered in a timely manner.

#### Background

OCC believes that its membership criteria are objective standards that are designed not to unfairly discriminate in the admission of participants to OCC,<sup>4</sup> as well as to provide for fair and open access to OCC.<sup>5</sup> Currently, the authority to approve or disapprove new applications for clearing membership resides with the Board.<sup>6</sup> Under Article V, Section 2 of OCC's By-Laws, OCC's Risk Committee, including its designated delegates or agents, is

responsible for reviewing applications for clearing membership, and the Risk Committee is responsible for making a recommendation of approval or disapproval to the Board (in part, relying on OCC's Management's review and recommendation).<sup>7</sup> OCC's management ("Management") performs the substantive review of applications for clearing membership on behalf of the Risk Committee. Management reviews a given application against OCC's membership criteria, which are set forth in Article V of OCC's By-Laws as well as Chapters 2 and 3 of OCC's Rules. Based on its review, Management, as the subject matter expert on OCC's membership criteria, either recommends an application for approval without conditions, recommends an application for approval with conditions (in accordance with OCC's By-Laws, Article V, Section 1, Interpretation and Policy .06), or does not recommend an application for approval. The Risk Committee, based on Management's review of the application, recommends a course of action to OCC's Board. OCC's Board then approves or disapproves applications for clearing membership based on the Risk Committee's recommendation.

Moreover, since the rules of the Commission and the Commodity Futures Trading Commission require OCC to have rules that do not unfairly discriminate in the admission of participants and provide fair and open access,<sup>8</sup> OCC believes that, under its rules, it is required to admit applicants for clearing membership that clearly meet OCC's membership criteria, and therefore, that the Board's ultimate approval of an application for clearing membership for which Management does not recommend approval with conditions or disapproval is pro forma. From a timing perspective, applications for clearing membership often do not track the Risk Committee or Board's regular meeting schedule and, on occasion, the Board has had to convene a special meeting for the sole purpose of considering an application for clearing membership or otherwise has had to seek approval via unanimous written consent, which OCC believes is an inefficient use of the Board's time and resources. In an effort to better allocate

the time and resources of OCC's Board and Risk Committee as well as streamline its clearing membership approval process, OCC proposed the amendments to Articles V and VIII of its By-Laws as well as the Board and Risk Committee Charters described below. The effect of such amendments is that either OCC's Executive Chairman or President will approve most applications for clearing membership, thereby allowing the Board and the Risk Committee to better allocate their time and resources.

#### *Changes to Vest Authority of New Applicant Approvals With the Risk Committee*

OCC proposed amending Article V, Section 2 of its By-Laws to vest the authority to approve or disapprove new applicants for clearing membership with the Risk Committee. OCC believes that the members of the Board comprising the Risk Committee are capable of appropriately acting on membership applications. The Risk Committee is currently delegated the authority to (1) review applications for clearing membership and recommend approval or disapproval thereof to the Board, (2) conduct hearings if requested by applicants whose applications are proposed to be disapproved, and (3) review and approve or disapprove requests by clearing members to expand clearing activities.<sup>9</sup> Therefore, OCC believes that requiring the Board to approve or disapprove an application for clearing membership that has already been reviewed by, and received a recommendation for approval or disapproval from, the Risk Committee is redundant and represents an inefficient use of the Board's time. Accordingly, OCC believes that the Risk Committee is the appropriate governing body in which to vest ultimate authority to approve or disapprove applications for clearing membership.<sup>10</sup> Should the Risk Committee propose to disapprove an application for clearing membership, the Risk Committee must first provide the applicant an opportunity to be heard and present evidence on its own behalf (as is currently the case today with respect to the Board's decision to

<sup>9</sup> See Section IV of the Risk Committee Charter provided as Exhibit 5B to the proposed rule change.

<sup>10</sup> The Board will continue to oversee OCC's membership criteria and ongoing membership standards through its authority to approve changes to OCC's By-Laws and Rules (and specifically those By-Laws and Rules that concern membership). The Risk Committee will inform the Board, at the Board's next regularly scheduled meeting, of applications for clearing membership pursuant to proposed Article V, Section 2(c) of the By-Laws.

<sup>3</sup> OCC's Risk Committee is a committee of OCC's Board of Directors. See OCC's By-Laws Article III, Section 9.

<sup>4</sup> See 15 U.S.C. 78q-1(b)(3)(F).

<sup>5</sup> See 7 U.S.C. 7a-1(c)(2)(C)(iii)(III).

<sup>6</sup> See OCC's By-Laws Article V, Section 2.

<sup>7</sup> See OCC's By-Laws Article V, Section 2. The Risk Committee, from a practical perspective, has designated OCC's management as its agent to review applications for clearing membership. OCC's management reviews applications for clearing membership and makes a recommendation to the Risk Committee concerning the applicant's satisfaction of OCC's membership criteria.

<sup>8</sup> See 15 U.S.C. 78q-1(b)(3)(F) and 7 U.S.C. 7a-1(c)(2)(C).

disapprove an application for clearing membership).<sup>11</sup>

In order to effect the foregoing, and in addition to proposed changes to Article V, Section 2 of the By-Laws, OCC proposed conforming changes to Article V, Sections 1 and 3 of the By-Laws as well as the Board and Risk Committee Charters.<sup>12</sup> Such conforming changes identify that the Risk Committee, and not the Board, will approve applications for clearing membership. Additionally, OCC proposed changes to Article VIII, Section 2 of the By-Laws (as well as the Board and Risk Committee Charters) to identify that the Risk Committee, and not the Board, will set initial clearing fund requirements in connection with the approval of an application for clearing membership.

*Delegation of Authority To Approve Applications for Membership to the Executive Chairman or President of OCC*

OCC has stated that, in order to better streamline OCC's membership application approval process, and allow the Board and the Risk Committee to more efficiently allocate their time, it proposed additional amendments to Article V, Section 2 of its By-Laws to allow OCC's Executive Chairman or its President to approve certain applications for clearing membership. As described above: (i) OCC believes that, based on the applicable rules of the Commission and the Commodity Futures Trading Commission, applications for clearing membership that clearly meet OCC's membership criteria must be approved,<sup>13</sup> and (ii) applications for clearing members do not necessarily track the Risk Committee or Board's regular meeting schedule and, on occasion, the Board has had to convene in a special meeting for the sole purpose of considering a clearing member application or otherwise seek approval via unanimous written consent, which is not a good use of either the Board or the Risk Committee's time and resources. Therefore, OCC proposed amending Article V, Section 2 of its By-Laws to delegate the authority to approve applications for clearing membership to the Executive Chairman or President of

OCC provided that: (i) It is not recommended that the Risk Committee impose additional membership criteria upon the applicant pursuant to Section 1, Interpretation and Policy .06 of Article V of OCC's By-Laws, and (ii) the Risk Committee is given not less than five business days from the date it is notified by its designated delegates or agents that the Executive Chairman or President intends to approve a given application to determine that such application should be reviewed at a meeting of the Risk Committee and the Risk Committee has not requested that the application be reviewed at a meeting of the Risk Committee within such five day period. If five business days pass and no member of the Risk Committee notifies Management that a given application for clearing membership should be reviewed at a meeting of the Risk Committee, then the Executive Chairman and President shall have the authority to approve the application for clearing membership. This proposed change will allow either OCC's Executive Chairman or the President to approve most applications for clearing membership received by OCC. Neither the Executive Chairman nor the President will be allowed to disapprove an application for clearing membership. Instead, if either the Executive Chairman or President determined he cannot approve an application for clearing membership, the application will be considered by the Risk Committee for approval or disapproval at its next regularly scheduled meeting. OCC believes that allowing the Executive Chairman or President to approve applications for clearing membership that clearly meet OCC's membership criteria will allow the Board and the Risk Committee to allocate their time to more efficiently and effectively.

## II. Discussion

Section 19(b)(2)(C) of the Act<sup>14</sup> directs the Commission to approve a proposed rule change of a self-regulatory organization if it finds that the rule change, as proposed, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to such organization.

The Commission finds that the proposed rule change is consistent with Section 17A(b)(3)(F)<sup>15</sup> of the Act. This section requires, among other things, that the rules of a clearing agency be designed to protect investors and the public interest while not being designed

to permit unfair discrimination in the admission of participants. The proposed rule change will preserve Board-level oversight for the membership approval process by vesting the authority to approve or disapprove applications for clearing membership with the Risk Committee, a Board-level committee. A considerable portion of the Risk Committee's functions and responsibilities, as listed in its charter, pertains to the oversight of membership and membership standards generally. Therefore it is reasonable to expect that the Risk Committee should have the requisite expertise and authority to carry out the membership application approval or disapproval process previously tasked to the entire Board.

The proposed rules also delegate to the Executive Chairman or the President the authority to approve new applications provided that: (i) It is not recommended that the Risk Committee impose additional membership criteria upon the applicant pursuant to Section 1, Interpretation and Policy .06 of Article V of OCC's By-Laws, and (ii) the Risk Committee is given not less than five business days to determine that the application should be reviewed at a meeting of the Risk Committee and the Risk Committee has not requested that the application be reviewed at a meeting of the Risk Committee within such five day period. The authority to disapprove applications is not delegated to the Executive Chairman or the President. The rules, as revised, continue to provide Board-level oversight of the membership approval process by ensuring involvement of the Risk Committee. For the above reasons, although the revised rules will streamline the membership approval process, the Commission believes that they are designed to protect investors and the public interest. Additionally, the revised rules are not designed to permit unfair discrimination because they do not alter the criteria considered for the approval of new membership.

Additionally, the Commission finds that the revised rules are consistent with Rule 17Ad-22(d)(8) under the Act.<sup>16</sup> Rule 17Ad-22(d)(8) requires that a clearing agency establish, implement, maintain, and enforce written policies and procedures reasonably designed to, as applicable, have governance arrangements that are clear and transparent to fulfill the public interest requirements in Section 17A of the Act<sup>17</sup> applicable to clearing agencies and support the objectives of owners and participants. OCC's revised rules

<sup>11</sup> See OCC's By-Laws Article V, Section 2. Typically, however, if OCC's due diligence review reveals issues that would prevent the Board or the Risk Committee from approving an application for clearing membership, the applicant voluntarily remediates such issues prior to the presentation of the application for clearing membership to the Risk Committee.

<sup>12</sup> Marked versions of the Board and Risk Committee Charters were provided as Exhibits 5A and 5B to the proposed change.

<sup>13</sup> See 15 U.S.C. 78q-1(b)(3)(F) and 7 U.S.C. 7a-1(c)(2)(C).

<sup>14</sup> 15 U.S.C. 78s(b)(2)(C).

<sup>15</sup> 15 U.S.C. 78q-1(b)(3)(F).

<sup>16</sup> 17 CFR 240.17Ad-22(d)(8).

<sup>17</sup> 15 U.S.C. 78q-1.

provide clarity and transparency in its governance processes by identifying, in OCC's public rulebook, the parties authorized to approve or disapprove membership applications, and fulfill the public interest requirements of Section 17A of the Act as described above.

### III. Conclusion

On the basis of the foregoing, the Commission finds that the proposal is consistent with the requirements of Act, and in particular, with the requirements of Section 17A of the Act<sup>18</sup> and the rules and regulations thereunder.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>19</sup> that the proposed rule change (SR-OCC-2016-007) be, and it hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>20</sup>

**Robert W. Errett,**  
Deputy Secretary.

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-78289; File No. PCAOB-2007-04]

### Public Company Accounting Oversight Board; Order Granting Approval of Proposed Amendments to Board Rules Relating to Inspections

July 11, 2016.

#### I. Introduction

On March 24, 2016, the Public Company Accounting Oversight Board (the "Board" or the "PCAOB") filed with the Securities and Exchange Commission (the "Commission"), pursuant to Section 107(b)<sup>1</sup> of the Sarbanes-Oxley Act of 2002 (the "Sarbanes-Oxley Act") and Section 19(b)<sup>2</sup> of the Securities Exchange Act of 1934 (the "Exchange Act"), a proposal to adopt amendments to Rule 4003, *Frequency of Inspections*, to revise paragraphs (b) and (d) and add new paragraphs (e) and (h) (collectively, the "Proposed Rules").<sup>3</sup> The Proposed

<sup>18</sup> In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>19</sup> 15 U.S.C. 78s(b)(2).

<sup>20</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> 15 U.S.C. 7217(b).

<sup>2</sup> 15 U.S.C. 78s(b).

<sup>3</sup> On October 22, 2007, the Board filed amendments related to Rule 4003 with the Commission and requested Commission approval. The Commission did not act on the amendments

Rules were published for comment in the **Federal Register** on April 13, 2016.<sup>4</sup> At the time the notice was issued, the Commission extended to July 12, 2016 the date by which the Commission should take action on the Proposed Rules.<sup>5</sup> The Commission received two comment letters in response to the notice.<sup>6</sup> This order approves the Proposed Rules.

#### II. Description of the Proposed Rules

On February 26, 2016, the Board adopted amendments to Rule 4003 to (i) require that at least five percent of registered public accounting firms that play a substantial role in the preparation or furnishing of an audit report be inspected on an annual basis, (ii) maintain the requirement to inspect all firms that issue an audit report for an issuer but provide the Board the discretion to forego an inspection, on a case-by-case basis, for a firm that does not subsequently issue an audit report for two consecutive years, (iii) qualify the term "audit report" to keep relevant portions of the rule consistent with the original meaning, and (iv) specify that no inspection requirement arises solely because a firm consented to an issuer's use of a previously issued audit report.

##### *A. Amendments Related to the Inspection of Substantial Role Only Firms*

Under the Proposed Rules, the triennial inspection requirement for registered public accounting firms that play a substantial role in audits but do not issue audit reports ("substantial role only")<sup>7</sup> is eliminated and replaced with a requirement to inspect at least five percent of such "substantial role only" firms. As a result, Rule 4003(b) is amended to delete the references to "substantial role only" firms and Proposed Rule 4003(h) is added to

subject to the 2007 filing. On February 26, 2016, the Board adopted revisions to those proposed amendments and, on March 24, 2016 amended the 2007 filing to reflect those revisions.

<sup>4</sup> See Release No. 34-77558 (April 7, 2016), 81 FR 21909 (April 13, 2016).

<sup>5</sup> *Ibid.*

<sup>6</sup> See letters from Deloitte Touche Tohmatsu Limited, dated April 29, 2016 ("Deloitte"), available at <https://www.sec.gov/comments/pcaob-2007-04/pcaob200704-1.pdf>, and an anonymous letter, dated May 3, 2016 ("anonymous letter"), available at <https://www.sec.gov/comments/pcaob-2007-04/pcaob200704-2.htm>.

<sup>7</sup> We are using the phrase "substantial role only" to identify the registered public accounting firms that play a substantial role in audits of issuers but do not issue audit reports with respect to any issuers as distinguished from the category of firms that play a substantial role in some audits and separately issue audit reports with regards to other audits. Firms that play a substantial role in an audit of an issuer must register with the PCAOB. See PCAOB Rule 2100(b).

require that the Board will inspect at least five percent of the "substantial role only" firms on an annual basis. Additionally, Rule 4003(d) is amended to remove the references to "substantial role only" firms.

##### *B. Amendments Related to the Inspections of Firms That Have Not Issued Audit Reports in Two Consecutive Years*

Under the Proposed Rules, Rule 4003(b) will continue to retain the requirement to inspect any registered public accounting firm that issues an audit report with respect to an issuer. However, Proposed Rule 4003(e) is added to provide the Board with the discretion to forego the inspection of a registered public accounting firm that has not issued any audit reports in two consecutive years.

##### *C. Amendments Related to the Term "Audit Report" and Consents to the Use of Previously Issued Audit Reports*

Under the Proposed Rules, Rule 4003(d) is amended to add the phrase "with respect to an issuer" to qualify the term "audit report" within the rule. The added qualification is needed to clarify that the Proposed Rules apply only to the audits of issuers because, after the original rule was adopted, the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act")<sup>8</sup> amended the Sarbanes-Oxley Act to establish the PCAOB's oversight of the audits of broker-dealers.<sup>9</sup> Additionally, Rule 4003(b) is amended to provide that no inspection requirement arises under the rule solely because a firm consents to an issuer's use of a previously issued audit report.

##### *D. Applicability and Effective Date*

The Proposed Rules would become effective upon approval by the Commission and apply to the audits of all issuers, including audits of emerging growth companies ("EGCs"),<sup>10</sup> as discussed in Section IV below. The Proposed Rules do not impact the inspection frequency of the audits of brokers and dealers under Exchange Act Rule 17a-5.<sup>11</sup>

### III. Comment Letters

As noted above, the Commission received two comment letters

<sup>8</sup> Public Law 111-203, 124 Stat. 1376 (2010).

<sup>9</sup> See Section 101 of the Sarbanes-Oxley Act [15 U.S.C. 7211].

<sup>10</sup> The term "emerging growth company" is defined in Section 3(a)(80) of the Exchange Act [15 U.S.C. 78c(a)(80)].

<sup>11</sup> If the broker or dealer is also an issuer, the Proposed Rules could impact the inspection frequency of the audits of such broker or dealer.