

**MEMO# 30539**

January 25, 2017

# **CFTC Proposes Amendments to Recordkeeping Rule to Reflect Changes in Technology; Member Call on February 3, 2017**

[30539] January 25, 2017 TO: Derivatives Markets Advisory Committee  
Registered Fund CPO Advisory Committee RE: CFTC Proposes Amendments to  
Recordkeeping Rule to Reflect Changes in Technology; Member Call on February 3, 2017

Recently, the Commodity Futures Trading Commission (“CFTC” or “Commission”) proposed amendments (“Proposal”)[[1](#)] to rule 1.31 under the Commodity Exchange Act (“CEA”), which governs recordkeeping requirements under the CEA and Commission rules. The Proposal, which was issued in response to petitions for rulemaking from ICI and other trade associations,[\[2\]](#) is summarized below.

**Comments on the Proposal are due March 20, 2017. ICI will hold a member call on Friday, February 3, at 2 pm ET to discuss possible comments on the Proposal. You should have received an Outlook invitation directly for the call that includes dial-in information. If you did not, and would like to participate in the call, please contact Jennifer Odom at [jodom@ici.org](mailto:jodom@ici.org) or (202) 326-5833.**

## **Background**

Rule 1.31 sets out the recordkeeping requirements for all books and records required to be kept under the CEA and Commission rules, unless otherwise provided, and implements the Commission’s inspection and examination authority over those records. Paragraph (a) of the rule requires that books and records generally be kept for five years, and be readily accessible during the first two years. Records of any swap or related cash or forward transaction must be kept until the termination, maturity, expiration, transfer, assignment or novation date of the transaction and for a period of five years thereafter, and records of oral communications must be kept for a period of one year. The rule requires that paper records be kept in their original form and electronic records in the form in which they were originally created (“native file format”). The rule also provides for the inspection and production rights of representatives of the CFTC and Department of Justice.

Paragraph (b) of the rule allows books and records to be stored on microfilm or similar media, or electronic storage media, provided that the recordkeeper satisfy technical requirements designed to ensure the integrity, availability, and accessibility of the

information. For example, for electronic records, the storage media must preserve the native file format of the electronic records, and the records must be preserved in a non-rewritable, non-erasable (“write-once, read-many” or “WORM”) form and meet other specified requirements. The rule also provides that a person who uses only electronic storage media to preserve some or all of its records must enter into an arrangement with a third party technical consultant (“Technical Consultant”) capable of furnishing to the CFTC or its representative any information stored electronically promptly upon request.

Paragraph (c) of rule 1.31 requires recordkeepers to provide notice and a representation to the CFTC prior to the initial use of an electronic record storage system. Paragraph (d) requires that certain paper records, such as trading cards and documents with written trading information, must be maintained in hard copy for the applicable retention period.

In March 2014, ICI submitted a rulemaking petition to the CFTC that requested that the Commission amend (i) rule 4.12(c) under the CEA, which contains exemptions from Subpart B of the Commission’s Part 4 rules, (ii) rule 4.23 under the CEA, which contains recordkeeping requirements applicable to commodity pool operators (“CPOs”), and (iii) rule 4.33 under the CEA, which contains recordkeeping requirements applicable to commodity trading advisors (“CTAs”).<sup>[3]</sup> Rules 4.23 and 4.33 incorporate rule 1.31. ICI explained that registered fund CPOs and CTAs are subject to comprehensive recordkeeping requirements under the Investment Company Act of 1940 (“1940 Act”) and the Investment Advisers Act of 1940 (“Advisers Act”), and that additionally complying with the requirements of rules 4.23, 4.33, and the outdated technological requirements of rule 1.31 would be costly and burdensome. ICI therefore requested that the CFTC amend its recordkeeping rules to allow registered fund CPOs and registered fund CTAs to comply by satisfying the SEC’s recordkeeping rules (*i.e.*, substituted compliance).

## **The Proposal**

The Commission explains that, since rule 1.31 was last amended substantially in 1999, advances in information technology may have caused certain elements of the rule to become obsolete. It proposes to update the rule in a manner that would eliminate outdated provisions while still maintaining the Commission’s ability to examine and inspect required records. The Proposal is intended to be technology neutral, in order to withstand changes to technology over time.

## **Scope**

The Proposal seeks to provide greater clarity regarding applicability of the recordkeeping obligations under rule 1.31. Under the Proposal, rule 1.31 would apply to a “records entity,”<sup>[4]</sup> which may include a “registered entity”<sup>[5]</sup> such as a derivatives clearing organization, designated contract market, swap execution facility, and swap data repository; a registrant such as a futures commission merchant, an introducing broker, a commodity pool operator, a commodity trading advisor, a floor broker, a floor traders a retail foreign exchange dealer, a swap dealer, and a major swap participant; as well as others that are neither registered entities nor registrants, such as traders that are subject to recordkeeping requirements under the CEA.

The Proposal would replace the rule’s current references to “books and records” with the term “regulatory records” and would differentiate between electronic and paper regulatory records.<sup>[6]</sup> The Proposal would further define the term “regulatory records” to clarify the existing requirement that a recordkeeper must maintain prior versions of a regulatory record, no matter how modified.<sup>[7]</sup> The Proposal also would require retention of metadata

relating to required records.”

### ***Policies and Procedures***

Rule 1.31(b) of the Proposal would revise and restate the ongoing compliance obligations regarding policies and procedures relating to recordkeeping under the rule. It would require all records entities to establish, maintain, and implement written policies and procedures reasonably designed to ensure that the records entity complies with its obligations under rule 1.31.

### ***Duration of Retention***

The Proposal would restate and clarify, in paragraph (c) of the rule, the existing retention period requirements for categories of regulatory records under rule 1.31. The Proposal would eliminate the requirement that paper records be maintained in their original form and that electronic records be maintained in native file format. A records entity would be required to retain records for the following time periods:

- Regulatory records of any swap or related cash or forward transaction,[\[8\]](#) other than regulatory records of oral communications, from the date the regulatory record was created until the termination, maturity, expiration, transfer, assignment, or novation date of the transaction and for a period of not less than five years after such date.
- A records entity that is required to retain oral communications would be required to retain such communications for a period of not less than one year from the date of such communication.
- All other regulatory records would be required to be maintained for a period of not less than five years from the date on which such record was created.
- Regulatory records exclusively created and maintained on paper would be required to be readily accessible for no less than two years. Electronic regulatory records would be required to be readily accessible for the duration of the required recordkeeping period.

### ***Form and Manner of Retention***

Proposed rule 1.31(d) would restate and revise certain requirements for records currently set forth in rule 1.31(b)(1)-(3). The Proposal generally would require that a records entity retain all regulatory records in a form and manner that ensures the records’ and recordkeeping systems’ authenticity and reliability. While the general requirement would not distinguish between paper and electronic records, records entities retaining electronic records would be required to meet several principal-based standards intended to ensure the security, integrity, and availability of the information in the records.[\[9\]](#) The Proposal does not specify specific electronic technologies that are permissible for recordkeeping, but instead describes the characteristics such systems and controls would need to have to satisfy the proposed authenticity and reliability standard. The Proposal would eliminate the requirements that a records entity preserve the native file format of the electronic records, and that the records be preserved in WORM format.

### ***Inspection and Production of Records***

The Proposal generally would restate the existing requirement in rule 1.31 that records under the rule are subject to inspection by representatives of the CFTC and the Department of Justice. The Proposal would amend the production requirements under rule 1.31 to

differentiate between the production of paper and electronic regulatory records. For records that are exclusively created and maintained on paper, proposed rule 1.31(e)(2) would require a records entity to produce the records promptly upon request. For electronic records, proposed rule 1.31(e)(3) would require a CFTC representative to specify a reasonable form and medium in which the records entity would be required to produce the records. Under the Proposal, the records would be required to be produced promptly, upon request, unless otherwise directed by the Commission representative. The Commission notes that, while the Proposal would not require that records be provided in their “native file format,” it is intended to ensure that a records entity produces records in the most useable form and medium.

### ***Technical Consultant***

The Proposal would remove the current requirement in rule 1.31 for a records entity that retains records electronically to enter into an arrangement with a Technical Consultant. The Commission agrees that it is not necessary for records entities electing to store information electronically to engage a third party to ensure compliance with electronic recordkeeping obligations.

### ***Other Proposed Changes***

The Proposal would remove the requirement in rule 1.31(c) that the records entity provide a written representation to the Commission relating to its use of electronic storage media. The Commission believes that the requirements in rule 1.31 regarding written policies and procedures for regulatory records make this provision unnecessary. The Proposal also would remove the provision in rule 1.31(d) that requires that certain paper records, such as trading cards and paper copies of electronically filed certified forms, must be retained in hard copy for the required time period. The Commission believes that this requirement is no longer necessary, given that the Proposal would provide increased flexibility regarding the form and manner in which entities may retain records.

The Commission explains that it is reviewing its rules for potential technical amendments related to the Proposal, including the part 4 rules cited by petitioners in their rulemaking petitions, and that that review may or may not result in a new proposed rulemaking.

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### **endnotes**

[1] *Recordkeeping*, 82 Fed. Reg. 6356 (Jan. 19, 2017), available at <http://www.cftc.gov/idx/groups/public/@lrfederalregister/documents/file/2017-01148a.pdf> (“Proposing Release”).

[2] See Petition for Rulemaking to Amend CFTC Regulations 4.12(c)(3), 4.23 and 4.33, by Investment Company Institute, dated March 11, 2014, available at <https://www.ici.org/pdf/27946.pdf> (“ICI Rulemaking Petition”); Petition for Rulemaking to Amend 1.31, 4.7(b) and (c), 4.23 and 4.33, Managed Funds Association, Investment Adviser Association, and Alternative Investment Management Association, dated July 21, 2014.

[3] ICI Rulemaking Petition, *supra* note 2.

[4] A “records entity” would be defined as “any person required by the Act or Commission regulations...to keep regulatory records.”

[5] See Section 1a(40) of the CEA.

[6] “Electronic regulatory records” would be defined as “all regulatory records other than paper regulatory records exclusively created and maintained by a records entity on paper.” The Commission notes that the Proposal does not address source code or the production of source code.

[7] Specifically, the Proposal would provide that, for electronic records, this also would include: “ (i) All data produced and stored electronically that describes, directly or indirectly, the characteristics of such books and records, including, without limitation, data that describes how, when, and, if relevant, by whom such electronically stored information was collected, created, accessed, modified, or formatted; and (ii) any data necessary to access, search, or display any such books and records.”

[8] As defined in CFTC rule 23.200(i).

[9] See proposed rule 1.31(d)(2). The Commission notes that these recordkeeping requirements are not new and are consistent with the requirements of rule 204-2(g)(3) under the Advisers Act and rule 31a-2(f) under the 1940 Act. Proposing Release, *supra* note 1, at n.24.