

MEMO# 29589

December 23, 2015

CFTC Adopts Amendments Excluding Commodity Trading Advisors from Oral Recordkeeping Requirement

[29589]

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TO: DERIVATIVES MARKETS ADVISORY COMMITTEE No. 92-15
REGISTERED FUND CPO ADVISORY COMMITTEE RE: CFTC ADOPTS AMENDMENTS
EXCLUDING COMMODITY TRADING ADVISORS FROM ORAL RECORDKEEPING REQUIREMENT

The Commodity Futures Trading Commission (“CFTC”) recently adopted amendments to Regulation 1.35(a) (“Final Rule”) under the Commodity Exchange Act (“CEA”), which addresses recordkeeping requirements applicable to certain market participants, including a member of a designated contract market (“DCM”) or a swap execution facility (“SEF”), with respect to transactions relating to their business of dealing in commodity interests. [\[1\]](#) Late last year, the CFTC proposed amendments to Regulation 1.35(a) (“Proposed Amendments”) that would, among other things, expand and make permanent the temporary no-action relief that the CFTC staff has granted to commodity trading advisors (“CTAs”) that are members of a DCM or SEF to exclude them from the requirement to record all oral communications that lead to the execution of a transaction in a commodity interest. [\[2\]](#) The Final Rule is summarized briefly below.

Relief for CTAs

Consistent with the Proposed Amendments and the prior no-action relief the CFTC staff has granted, [\[3\]](#) the Final Rule would exclude CTAs that are members of a DCM or of a SEF from the requirement to record and maintain oral communications that lead to the execution of a commodity interest transaction. The CFTC, however, declined to exempt CTAs from the requirement to keep records of written communications under Regulation 1.35, as requested by ICI and others. While the CFTC acknowledged that many CTAs that are members of a DCM or SEF have discretionary trading authority over customers’ accounts and, therefore would not have routine telephone conversations with customers that lead to the execution of a transaction in a commodity interest, it noted that some CTAs may execute an order on behalf of a customer on a non-discretionary basis. It further stated its belief that the costs of recording and maintaining written records are significantly less than the costs of recording and maintaining oral communications. After discussing the arguments ICI and others presented for exempting CTAs from Regulation 1.35’s written

recordkeeping requirements, the CFTC stated that its interest in “ensuring customer protection and market integrity justifies the incremental costs to maintain these and other records” under the Final Rule. [4]

Relief from Recordkeeping Form and Manner Requirements

Currently, Regulation 1.35(a) specifies that required records under the rule, including records of oral and written communications that lead to the execution of a transaction, must be maintained in a form and manner “identifiable and searchable by transaction.” The Final Rule amends that requirement so that required records must be kept in a form and manner that: (1) permits prompt, accurate and reliable location, access, and retrieval of any particular record, data or information, and (2) other than pre-trade communications, allows for identification of a particular transaction. The CFTC explained that, for purposes of the Final Rule, records are considered to “allow[] for identification of a particular transaction” when a market participant can identify those records that pertain to a particular transaction. [5]

Commenters had raised concerns that the Final Rule’s requirement that records be “searchable” may be inconsistent with the requirement in CFTC Regulation 1.31 that records be maintained in native file format. [6] The CFTC stated in the Adopting Release that these requirements do not conflict because the Final Rule does not require market participants to convert their records to searchable electronic databases. The CFTC explained that there is no prescribed methodology under the Final Rule by which records must be searched or retrieved – and records may be maintained in paper or electronic form – as long as searches yield “prompt, accurate and reliable location, access, and retrieval of any particular record, data, or information.” [7]

Exclusion of Unregistered Members from Certain Recordkeeping Requirements

The Final Rule excludes DCM and SEF members that are not registered or required to register with the CFTC (i.e., end-users) (“Unregistered Members”) from several key requirements under Regulation 1.35(a), including the requirements to: (1) maintain written pre-trade communications and (2) keep transaction records transmitted via text messages. The Final Rule specifies further that Unregistered Members are not required to keep their records in any particular form or manner. Thus, under the Final Rule, Unregistered Members are only required to keep records of their transactions in a commodity interest, not communications that lead to the execution of a commodity interest transaction and related cash or forward transactions.

Reorganization of Rule

The Final Rule also reorganized the text of Regulation 1.35(a) to provide greater clarity to CFTC registrants and Unregistered Members. The CFTC emphasized that this reorganization did not modify entities’ regulatory obligations under the Final Rule.

Sarah A. Bessin
Associate General Counsel

endnotes

[1] Records of Commodity Interest and Related Cash or Forward Transactions, available at <http://www.cftc.gov/idc/groups/public/@newsroom/documents/file/federalregister121815.pdf>

f (“Adopting Release”).

[2] For a summary of the Proposed Amendments, please see ICI Memorandum No. 28525 (Nov. 13, 2014), available at https://www.ici.org/my_ici/memorandum/memo28525. ICI submitted a comment letter on the Proposed Amendments on January 13, 2015. See ICI Memorandum No. 28659 (Jan. 13, 2015), available at https://www.ici.org/my_ici/memorandum/memo28659.

[3] See, e.g., CFTC Letter No. 15-65 (Dec. 8, 2015), available at <http://www.cftc.gov/idc/groups/public/@lrllettergeneral/documents/letter/15-65.pdf>. For a summary of that letter, please see ICI Memorandum No. 29538 (Dec. 10, 2015), available at https://www.ici.org/my_ici/memorandum/memo29538.

[4] Note that, consistent with the current rule, the Final Rule also requires commodity pool operators (“CPOs”) that are members of a DCM or SEF to maintain written pre-trade communications. Under the current rule, CPOs are only excluded from the requirement to record and maintain oral pre-trade communications. The CFTC did not explicitly address ICI’s request that the Final Rule exclude CPOs from Regulation 1.35’s requirements pertaining to written records but, as discussed above, made it clear it was unwilling to extend the relief in the Proposed Rules further in this regard.

[5] Adopting Release, *supra* note 1, at 9.

[6] Regulation 1.31, which sets out the general recordkeeping requirements applicable to entities subject to CFTC regulation, is directly referenced in Regulation 1.35, as well as in Regulation 4.33, the recordkeeping rule applicable to CTAs.

[7] Adopting Release, *supra* note 1, at 13.