ALERTS

CFTC Defers Effectiveness of Oral Recording Requirements for Registered Commodity Trading Advisors Holding SEF Memberships

December 23, 2013

On Dec. 21, 2013, the U.S. Commodity Futures Trading Commission issued broadly applicable no-action relief deferring (through May 1, 2014) the effectiveness of recordkeeping requirements that would have required fund managers registered as commodity trading advisors who hold swap execution facility memberships to preserve oral communications (including telephone calls) relating to any trading of commodity interests.

This relief, requested by the Asset Management Group of the Securities Industry and Financial Markets Association and the Managed Funds Association, covers "asset managers"[1] registered as CTAs, many of which are obtaining SEF memberships as a direct and necessary response to the Dodd-Frank Act's central clearing mandates.

The request for relief related to certain unanticipated effects of recent amendments to Regulation 1.35(a), a long-standing rule that imposed recordkeeping rules on a variety of CFTC registrants. The 2013 amendments, which were to go into effect on Dec. 21, were drafted to accommodate the new statutory framework for cleared swaps under the Dodd-Frank Act (including the creation of SEFs) which, by definition, preceded the actual formation of SEFs; some of the SEF documentation published subsequent to the amendments, when combined with other CFTC guidance, resulted in an effective conclusion that registered CTAs that hold SEF memberships are covered by the revised Regulation 1.35(a).

Revised Regulation 1.35(a) requires that registrants holding SEF memberships "keep full, complete, and systematic records … of all transactions relating to its business of dealing in commodity interests[;]" however, the rule also states that:

> [I]ncluded among the records required to be kept … are *all oral and written communications* provided or received concerning quotes, solicitations, bids, offers, instructions, trading, and prices that lead to the execution of a transaction in a commodity interest and related cash or forward transactions, *whether communicated by telephone, voicemail*, facsimile, instant messaging, chat rooms, electronic mail, mobile device, or other digital or electronic media. [Emphasis added.]

In the revised Regulation 1.35(a), the CFTC included an exclusion to the oral recordkeeping requirements for CPOs, but notably not for CTAs. Absent no-action relief, private fund managers (and others) that are registered CTAs[2] and that are members of SEFs would have had to implement systems to capture and classify voice communications related to *all* their commodity interest trading (and not limited to the trading done on a SEF).[3] Covered CTAs deemed this obligation to be onerous, unnecessary and potentially counterproductive and with this delay the CTFC will be examining those concerns more closely.

As noted above, this relief is time-limited and is effective through May 1, 2014.

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If you have any questions concerning this *Alert*, please contact your attorney at Schulte Roth & Zabel or one of the authors.

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[1] While "asset manager" is not a registration category or defined term under the Commodity Exchange Act or the regulations promulgated pursuant thereto, the CFTC accepted this definition provided by the two trade associations: "any person in the business of providing investment advice or advice regarding the value of securities or commodity interests for compensation and includes persons registered with the Securities and Exchange Commission or any U.S. state as an investment adviser under the Investment Advisers Act of 1940, any person registered with the Commission as a commodity trading advisor or commodity pool operator, any person regulated by a foreign regulatory authority as an investment

adviser and any person operating pursuant to an exemption or exclusion from registration with or regulation by any such regulators."

[2] Fund managers registered as CPOs would likely fall within the exemption in the current text; others are registered as CPOs and CTAs and could have elected, assuming that they could still satisfy one or more of the CTA exemptions (e.g., the fifteen-or-fewer-clients exemption in 4.14(a)(10)), to deregister as CTAs and therefore avoid being covered by this aspect of the recordkeeping obligation. For managers that trade in commodity interests and have a large number of clients, however, this relief is likely to be particularly well-received.

[3] New Rule 1.35(a) otherwise went into effect on Dec. 21 with respect to other CFTC registrants who are not CTAs and are covered by the rule.

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