



COMMODITY FUTURES TRADING COMMISSION

17 CFR Part 1

RIN 3038-AE23

Records of Commodity Interest and Related Cash or Forward Transactions

AGENCY: Commodity Futures Trading Commission.

ACTION: Final rule.

SUMMARY: The Commodity Futures Trading Commission (the “Commission” or “CFTC”) is amending Commission Regulation 1.35(a) to: provide that all records required to be maintained under this regulation must be maintained in a form and manner which permits prompt, accurate and reliable location, access, and retrieval of any particular record, data, or information; clarify that all records, except records of oral and written communications leading to the execution of a commodity interest transaction and related cash or forward transactions, must be kept in a form and manner that allows for identification of a particular transaction; exclude members of designated contract markets (“DCMs”) and of swap execution facilities (“SEFs”) that are not registered or required to register with the Commission (“Unregistered Members”) from the requirements to keep written communications that lead to the execution of a commodity interest transaction and related cash or forward transactions, keep text messages, and keep records in a particular form and manner; and exclude commodity trading advisors (“CTAs”) from the oral recordkeeping requirement (“Final Rule”).

DATES: Effective [INSERT DATE OF PUBLICATION IN THE FEDERAL REGISTER].

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SUPPLEMENTARY INFORMATION:

I. Background

The Commission amended Regulation 1.35(a) in December 2012 as part of a series of rulemakings intended to integrate certain existing Commission rules more fully with the framework created by the Dodd-Frank Wall Street Reform and Consumer Protection Act for swap dealers and major swap participants (the “2012 Amendment”).¹

Regulation 1.35(a) requires each futures commission merchant (“FCM”), retail foreign exchange dealer (“RFED”), introducing broker (“IB”), and member of a DCM or of a SEF to keep full, complete, and systematic records of all transactions relating to its business of dealing in commodity interest and related cash or forward transactions.² The Commodity Exchange Act (“CEA”) defines “member” as an individual, association, partnership, corporation, or trust – (i) owning or holding membership in, or admitted to membership representation on, the registered entity³ or derivatives transaction execution

¹ See Adaptation of Regulations to Incorporate Swaps—Records of Transactions, 77 FR 75523 (December 21, 2012) (“2012 Amendment Adopting Release”).

² 17 CFR 1.35(a)(1).

³ The term “registered entity” is defined in CEA section 1a(40) to include both DCMs and SEFs. See CEA sections 1a(40)(A) (DCMs) and (D) (SEFs).

facility; or (ii) having trading privileges on the registered entity or derivatives transaction execution facility.⁴

Regulation 1.35(a) requires FCMs, RFEDs, IBs, and members of a DCM or of a SEF to keep records of written communications that lead to the execution of a commodity interest transaction and related cash or forward transactions. Additionally, Regulation 1.35(a) includes a requirement to keep records of certain oral communications, which applies to each FCM, RFED, large IB (defined as an IB that has generated over \$5 million in aggregate gross revenues over the preceding three years from its activities as an IB), and member of a DCM or of a SEF that is registered or required to register with the Commission as a floor broker (“FB”) (only with regard to acting as an agent for a non-affiliated client) or as a CTA.⁵ Unlike the written recordkeeping requirement that applies to both commodity interest transactions and related cash or forward transactions, the oral recordkeeping requirement is limited to commodity interest transactions.⁶ The scope of records covered by Regulation 1.35(a) includes communications by telephone, voicemail, facsimile, instant messaging, chat rooms, electronic mail, mobile device, or other digital or electronic media.⁷ These communications include text messages.

⁴ 7 U.S.C. 1a(34).

⁵ As stated in the 2012 Amendment, the oral recordkeeping requirement in Regulation 1.35(a) does not apply to: (i) oral communications that lead solely to the execution of a related cash or forward transaction; (ii) oral communications provided or received by a floor broker that do not lead to the purchase or sale for any person other than the floor broker of any commodity for future delivery, security futures product, swap, or commodity option authorized under section 4c of the Commodity Exchange Act; (iii) an introducing broker that has generated over the preceding three years \$5 million or less in aggregate gross revenues from its activities as an introducing broker; (iv) a floor trader; (v) a commodity pool operator; (vi) a swap dealer; (vii) a major swap participant; or (viii) a member of a DCM or SEF that is not registered or required to be registered with the Commission in any capacity. 17 CFR 1.35(a)(1).

⁶ 17 CFR 1.35(a)(1).

⁷ Id.

Regulation 1.35(a) also mandates that all records be kept in a form and manner identifiable and searchable by transaction.

The 2012 Amendment became effective on February 19, 2013.⁸ Shortly thereafter, a variety of market participants began raising concerns regarding the practical impact of the rule, including its impact on non-financial commercial end-users. Commission staff hosted an End-User Roundtable Discussion on April 3, 2014 to discuss these concerns with affected parties. Commission staff subsequently issued no-action letters that addressed certain of the issues with the 2012 Amendment. CFTC Staff Letter No. 14-72 provided temporary no-action relief to Unregistered Members, relieving them from the requirements to (i) maintain text messages; and (ii) maintain records in a form and manner identifiable and searchable by transaction.⁹ CFTC Staff Letter No. 14-60 provided temporary no-action relief to CTAs that are members of a DCM or of a SEF, relieving them from the requirement to maintain records of oral communications in connection with the execution of swaps.¹⁰ CFTC Staff Letter No. 14-147 extended the temporary no-action relief provided to CTAs in CFTC Staff Letter No. 14-60, and expanded the scope of the relief to include oral communications that lead to the execution of a commodity interest transaction, in addition to communications that lead to the execution of a swap transaction.¹¹

⁸ 2012 Amendment Adopting Release at 75524.

⁹ CFTC Staff Letter No. 14-72, available at <http://www.cftc.gov/ucm/groups/public/@lrlettergeneral/documents/letter/14-72.pdf>.

¹⁰ CFTC Staff Letter No. 14-60, available at <http://www.cftc.gov/ucm/groups/public/@lrlettergeneral/documents/letter/14-60.pdf>.

¹¹ CFTC Staff Letter No. 14-147, available at <http://www.cftc.gov/ucm/groups/public/@lrlettergeneral/documents/letter/14-147.pdf>. Commission staff recently extended the relief in CFTC Staff Letter No. 14-147 until the effective date of any final Commission action with respect to the Proposed Amendment. See CFTC Staff Letter No. 15-65, available at <http://www.cftc.gov/ucm/groups/public/@lrlettergeneral/documents/letter/15-65.pdf>.

II. The Proposal

On November 14, 2014, the Commission published for comment in the Federal Register a proposal to amend Regulation 1.35(a) (the “Proposed Amendment” or “Proposal”) to: (i) provide that all records required to be maintained under the regulation must be searchable; (ii) clarify that all records must be kept in a form and manner that allows for identification of a particular transaction, except that records of oral and written communications leading to the execution of a commodity interest transaction and related cash or forward transactions are not required to be kept in a form and manner that allows for the identification of a particular transaction; (iii) exclude Unregistered Members from the requirements to retain text messages and to maintain records in a particular form and manner; and (iv) exclude CTAs from the oral recordkeeping requirement.¹²

III. Discussion

The Commission received 18 comment letters in response to the Proposal. The commenters represented a variety of interests, including eight commercial end-user trade groups, five advisor and broker trade groups, two exchanges, one technology vendor, one mortgage lending association, and one self-regulatory organization.¹³ After carefully considering all of the comments received, the Commission is adopting the Final Rule

¹² See Notice of proposed rulemaking: Records of Commodity Interest and Related Cash or Forward Transactions, 79 FR 68140 (November 14, 2014).

¹³ Comment letters were received from American Gas Association (“AGA”), Commodity Markets Council (“CMC”), Commercial Energy Working Group (“CEWG”), Coalition of Physical Energy Companies (“COPE”), Edison Electric Institute (“EEI”), Federal Home Loan Banks (“FHLB”), Investment Adviser Association (“IAA”), Intercontinental Exchange (“ICE”), Investment Company Institute (“ICI”), International Energy Credit Association (“IECA”), Managed Funds Association (“MFA”), Minneapolis Grain Exchange (“MGEX”), National Rural Electric Cooperative Association and American Public Power Association (Joint letter, “NRECA & APPA”), National Council of Farmer Cooperatives (“NCFC”), National Futures Association (“NFA”), National Introducing Brokers Association (“NIBA”), Asset Management Group of the Securities Industry and Financial Markets Association (“SIFMA AMG”), Voitrax Corporation (“Voitrax”). Public comments may be viewed on the Commission’s website at: <http://comments.cftc.gov/PublicComments/CommentList.aspx?id=1538>.

largely as proposed, with two exceptions. First, the Commission is clarifying the requirements governing the form and manner in which records must be kept. Second, the Commission is excluding Unregistered Members from the requirement to keep written communications that lead to the execution of a commodity interest transaction and related cash or forward transactions (in addition to adopting the proposed exclusions of Unregistered Members from the requirements to retain text messages and to maintain records in a particular form and manner).¹⁴

A. Proposal to Clarify the “Identifiable” and “Searchable” Requirements of the Rule Generally and to No Longer Require that Pre-Trade Communications Be Identifiable by Transaction

Regulation 1.35(a) mandates that required records, including records of oral and written communications that lead to the execution of a transaction, be maintained in a form and manner “identifiable and searchable by transaction.”¹⁵ Prior to the publication of the Proposed Amendment, the Commission received numerous requests for guidance regarding compliance with this form and manner requirement.¹⁶ Therefore, the Commission proposed to clarify the rule by stating that all required records must be searchable, but not “searchable by transaction.”¹⁷ The Commission further proposed to replace the requirement in Regulation 1.35(a) that records be “identifiable” with the

¹⁴ NFA and NIBA both requested that the Commission consider raising the revenue threshold that exempts small introducing brokers from the requirement to record oral communications. Neither proposed a specific alternate threshold. The Commission is not revising the revenue threshold for defining “small” introducing brokers for the purposes of the rule, as such a revision is outside of the scope of this rulemaking.

¹⁵ 17 CFR 1.35(a)(1).

¹⁶ See Proposal at 68143.

¹⁷ Id.

requirement that records be “kept in a form and manner that allows for the identification of a particular transaction.”¹⁸

In considering the Proposed Amendment, the Commission noted that access to searchable pre-trade communications is an important element of its oversight of the derivatives market and enforcement of Commission rules and regulations.¹⁹ The Commission recognized, however, that keeping these records in a form and manner that allows for the identification of a particular transaction could pose significant challenges to some market participants.²⁰ Therefore, the Commission also proposed to amend Regulation 1.35(a) to state that, although they still must be searchable, records of oral and written communications that lead to the execution of a transaction are not required to be kept in a form and manner that allows for identification of a particular transaction.²¹ This proposed change meant that market participants would not have to link or otherwise identify a record of a communication that leads to the execution of a transaction with a particular transaction.

i. Comments on Form and Manner Generally

Many commenters generally supported the proposed changes to the form and manner requirements of the rule, although some stated that the Commission should further clarify certain terms. AGA stated that the “searchable” and “identifiable” components of the Proposed Amendment are undefined terms that could create confusion. SIFMA AMG recommended that the Commission adopt an interpretation of “searchable” that is similar to the approach of the Securities and Exchange Commission

¹⁸ Id.

¹⁹ Id.

²⁰ Id.

²¹ Id.

(“SEC”), which does not prescribe any particular methodology. SIFMA AMG argued that this flexible application of the term would enable firms to adopt new technology and preserve records in a cost-effective manner without impeding regulatory oversight.

Voitrax, a technology company, did not support the Proposed Amendment, stating that it was developing low-cost technology which would make the rule’s existing requirement that records be “identifiable and searchable by transaction” both feasible and cost-effective. Voitrax stated that the Proposed Amendment’s standalone requirement that records be searchable (rather than indexed) is not cost-effective, and that “at higher volumes searching becomes infeasible.” Voitrax also noted that it had devoted significant resources to creating software to address the requirements in the 2012 Amendment, and if the Proposed Amendment is finalized, there may be a disincentive for companies to invest in technology solutions related to regulatory requirements in the future.

In the Commission’s view, records are “searchable” when they are kept in a form and manner which permits prompt, accurate and reliable location, access, and retrieval of any particular record, data, or information.²² Therefore, with respect to the form and manner in which records are required to be kept, the Commission is replacing the term “searchable” with the phrase “maintained in a form and manner which permits prompt, accurate and reliable location, access, and retrieval of any particular record, data, or information.” Further, the Commission is clarifying that for the purpose of this rule, records “allow for identification of a particular transaction” when a market participant can identify those records that pertain to a particular transaction.

²² The Commission observes that these requirements are substantially similar to those contained in the SEC rules for investment adviser recordkeeping. See 17 CFR 275.204-2(g)(2).

The Commission notes that the Final Rule does not require market participants to convert their records to searchable electronic databases. Rather, the Final Rule is deliberately drafted in a way that permits market participants subject to the rule to keep their paper and electronic records in a manner which they deem prudent and appropriate for their particular business. There is no prescribed methodology under Regulation 1.35(a) by which records must be searched or retrieved, so long as those searches yield prompt, accurate and reliable location, access, and retrieval of any particular record, data, or information.

The Commission has carefully considered Voitrax's comment opposing the Proposed Amendment, but disagrees with Voitrax's contention that the requirement that records be searchable is not cost-effective, and is also infeasible at high volumes. As explained above, the Commission notes that the Final Rule does not prescribe any particular methodology or corresponding technology with which records must be searchable; rather, the rule can be satisfied using a variety of approaches with varying costs. The Commission also acknowledges Voitrax's concern that the Commission's changes to an existing rule may create a disincentive for some firms to develop technology to address Commission rules. Any rule amendment may have some effect on market participants, as well as the vendors that support those market participants. In this case, the Commission has tailored the rule to address some concerns that market participants have presented in a manner consistent with the overall purpose of the rule. Although Voitrax disagreed with the Proposed Amendment, the Commission believes that the Final Rule preserves the core market integrity and customer protection aspects of

the rule, while reducing certain elements of the recordkeeping obligations imposed by the rule.²³

ii. Comments Addressing Regulation 1.31

Regulation 1.35(a) states that market participants “shall retain the records required to be kept by this section in accordance with the requirements of § 1.31.”²⁴

Although the Commission did not propose to amend Regulation 1.31 in connection with the Proposed Amendment, several commenters raised concerns regarding the perceived incompatibility of Regulation 1.35(a) and Regulation 1.31.²⁵ In particular, many commenters stated that the requirement under Regulation 1.35(a) that records be “searchable” conflicts with the requirement in Regulation 1.31 that records be maintained in native file format.²⁶ Some commenters stated that reconciling these requirements was “impossible” or “practically impossible,” while another commenter stated that it would require a substantial investment in technology to obtain such functionality.²⁷

Commenters proposed several solutions to address these perceived inconsistencies. AGA suggested that Regulation 1.35(a) should not contain any form and manner requirements, and that form and manner should be dictated solely by Regulation 1.31. Further, AGA proposed a safe harbor for end-users to rely on the record retention

²³ The Commission notes that the technology described in Voitrax’s Comment Letter may still be useful in helping market participants comply with the form and manner requirements prescribed in the Final Rule.

²⁴ 17 CFR 1.35(a)(1).

²⁵ See AGA, CMC, EEI, IAA, MFA, MGEX, and SIFMA AMG Comment Letters. See also 17 CFR 1.31. Regulation 1.31 sets forth the form and manner in which all books and records required to be kept by the Commodity Exchange Act or Commission Rules must be maintained. Among other things, it mandates that records “shall be kept in their original form (for paper records) or native file format (for electronic records) for a period of five years from the date thereof and shall be readily accessible during the first 2 years of the 5-year period.” The rule also requires all market participants who exclusively use electronic storage for some or all of their records to employ at least one third-party technical consultant to manage the storage of those records. Some Unregistered Members raised interpretive questions regarding Regulation 1.31, a rule which they may not otherwise be subject to absent their inclusion in Regulation 1.35.

²⁶ See CMC, IAA, MFA, MGEX, and SIFMA AMG Comment Letters.

²⁷ See CMC, MFA, and MGEX Comment Letters.

performed by a DCM, SEF, or a CFTC-registered counterparty, with respect to any of the records required under Rules 1.35(a) and 1.31. They proposed that in the absence of a safe harbor, the Commission should add language to the rule stating that it would consider “good faith compliance” with recordkeeping rules as a mitigating factor when exercising its enforcement authority. CMC proposed that members of DCMs or of SEFs that are not fiduciaries should be excluded from the requirement that records required to be maintained pursuant to Regulation 1.35(a) be kept in accordance with Regulation 1.31. MGEX proposed eliminating the “searchable” and “identifiable” requirements from Regulation 1.35(a). As an alternative, they supported keeping the searchable requirement in Regulation 1.35(a) in conjunction with a significant amendment to Regulation 1.31 regarding the storage of electronic communications.

MFA noted that it, along with IAA and the Alternative Investment Management Association (“AIMA”), submitted to the Commission a petition for rulemaking (“1.31 Petition”) to amend Regulation 1.31 to be, among other things, “more flexible with regard to permitted formats.”²⁸ MFA stated that in the event the Proposed Amendment is finalized prior to any Commission action regarding the 1.31 Petition, the Commission should provide interim relief to CPOs and CTAs that are members of a DCM or of a SEF from the requirements of Regulation 1.31. They also suggested that the Commission grant substituted compliance with the SEC’s electronic recordkeeping requirements for those CFTC-registered CTAs and CPOs that are also SEC-registered investment advisers. Absent this relief, MFA asserted that these entities “will have to institute recordkeeping requirements that are obsolete or unworkable.” Similarly, SIFMA AMG requested that

²⁸ See Petition for Rulemaking to Amend CFTC Regulations 1.31, 4.7(b), and (c), 4.23 and 4.33, attached to MFA Comment Letter.

the Commission grant temporary no-action relief to all asset managers that are members of a DCM or of a SEF, including all CPOS and CTAs, from compliance with Rule 1.31 pending the Commission's consideration of the 1.31 Petition.

The Commission is aware that some commenters are concerned with the relationship between the requirements of Regulations 1.35(a) and 1.31. The Commission notes that most of the comments in this area centered on perceived inconsistencies with the requirement in Regulation 1.35(a) that records be searchable. The Commission believes that the clarification of the form and manner requirements of Regulation 1.35(a), as stated above, should allay some commenters' concerns regarding compliance with both rules. Searchable records are indispensable to the Commission's ability to conduct surveillance inquiries and investigations in an efficient and effective manner for the protection of customers and ensuring market integrity. For example, searchable records facilitate the timely pursuit of potential violations, which can be important in seeking to freeze and recover any customer funds received from illegal activity or address market disruptions. As noted above, the Commission reiterates that the Final Rule does not require market participants to convert their records to searchable electronic databases. Rather, this rule was deliberately drafted in a way that permits market participants to maintain their paper and electronic records in a manner which they deem prudent and appropriate for their particular business. There is no prescribed methodology under Regulation 1.35(a) by which records must be searched or retrieved, so long as those searches yield prompt, accurate and reliable location, access, and retrieval of any particular record, data, or information.

B. Proposal to Exclude Unregistered Members from the Requirements to Retain Text Messages and to Maintain Required Records in a Particular Form and Manner

i. Text Messages and the Form and Manner Requirement

Regulation 1.35(a) generally mandates that the market participants subject to its requirements retain records that are transmitted by, among other things, telephone, mobile device, or other digital or electronic media.²⁹ This includes text messages.³⁰ Prior to the publication of the Proposed Amendment, many end-users told the Commission that text messages were a primary means of communication for their commodity trading businesses. They stated, however, that it was prohibitively expensive to retain those records.³¹ In considering the Proposed Amendment, the Commission observed that its oversight of the derivatives market would not be unduly affected if Unregistered Members were not required to retain text messages.³² Therefore, the Commission proposed to exclude Unregistered Members from the requirements in Regulation 1.35(a) to retain text messages.

As discussed above, Regulation 1.35(a) also requires that all records be kept in a form and manner that is “identifiable and searchable by transaction.”³³ Prior to the publication of the Proposed Amendment, many end-users stated that it was difficult to maintain their records in this particular format due to the nature of the relationship between their cash or forward transactions and their trading and hedging practices in the

²⁹ 17 CFR 1.35(a)(1).

³⁰ Id.

³¹ See Proposal at 68143.

³² Id.

³³ 17 CFR 1.35(a)(1).

derivatives market.³⁴ The Commission had previously stated that the requirements that records be “searchable” and “identifiable” do not require entities to link all of their transactions in commodity interests to related cash or forward transactions by a specific identifier.³⁵ However, in considering the Proposed Amendment, the Commission noted that these form and manner requirements may nonetheless impose additional burdens on some Unregistered Members.³⁶ The Commission recognized that excluding Unregistered Members from the requirement to maintain their records in a particular form and manner may impose an incremental burden on the Commission. However, the Commission observed that as long as those entities were required to retain their records, this exclusion would not unduly compromise the Commission’s ability to oversee the derivatives market.³⁷ Therefore, the Commission also proposed to exclude Unregistered Members from the requirement in Regulation 1.35(a) to maintain records in a particular form and manner.³⁸

In response, the Commission received comments from representatives of commercial end-users in the agriculture and energy industry, two exchanges, one advisor trade group, and a mortgage lending association.³⁹ These commenters were supportive of these aspects of the Proposal related to Unregistered Members, but all contended that the Commission did not go far enough in its proposed relief.

Regarding the proposal to exclude Unregistered Members from the requirement to keep text messages, several commenters asked the Commission to clarify the term “text

³⁴ See Proposal at 68143.

³⁵ Id.

³⁶ Id.

³⁷ Id.

³⁸ Id.

³⁹ See CMC, NCFC, AGA, CEWG, COPE, EEL, IECA, NRECA & APPA, ICE, MGEX, SIFMA AMG and FHLB Comment Letters.

message.”⁴⁰ AGA requested that the Commission eliminate what it characterized as the “arbitrary distinction” the rule makes between text messages and other forms of real-time communications, including instant messaging and chat rooms. EEI, IECA, NRECA, and APPA requested further guidance on what types of communications qualify as text messages. In response to commenter requests to define the “text message,” the Commission is clarifying that the term “text message,” for the purposes of this rule, means any written communication sent from one telephone number to one or more telephone numbers by short message service (“SMS”) or multimedia messaging service (“MMS”), and not those written communications exchanged by proprietary messaging services. Proprietary messaging services are internet-based, which enables users to send and store messages interchangeably on mobile devices and computers, whereas SMS and MMS messages are traditionally only sent and stored on a mobile device.

Given that some Unregistered Members have informed the Commission that they conduct their commodity interest and related cash or forward transactions primarily via text message, it may be unduly burdensome to require them to implement the additional technology to allow these messages to be stored on computers. Registered market participants, on the other hand, tend to rely more heavily on other forms of communication to execute commodity interest transactions and related cash or forward transactions. To the extent these registered market participants choose to avail themselves of the ability to use text messages, they could more easily expand their existing communications retention infrastructure to include text message storage.

⁴⁰ See AGA, EEI, IECA, and NRECA & APPA Comment Letters.

ii. Written Communications that Lead to the Execution of a Transaction

Commenters representing commercial end-users also raised issues regarding an element of the existing rule which the Commission had not proposed to change. Specifically, the commenters addressed the requirement that firms maintain records of communications that “lead to” the execution of a commodity interest transaction and related cash or forward transactions. Several commenters stated that market participants cannot readily identify which communications will “lead to” the execution of transactions in commodity interests and related cash or forward transactions. Market participants therefore may be forced to retain every communication related to their commodity trading business.⁴¹ AGA stated that the “cumbersome and costly” requirement to retain all communications that lead to the execution of a transaction will deter market participants from participating on exchanges. AGA and CEWG suggested that Unregistered Members should not have to retain records of pre-trade communications; rather, they should only be required to retain written records of a final agreement or those that contain the material economic terms of a transaction.

The Commission has previously stated that records of communications that lead to the execution of a transaction can serve to protect market participants and promote the integrity of the markets.⁴² However, the Commission is persuaded that the nature of the activities of many Unregistered Members in the commodity interest markets – which activities predominantly involve the hedging of risks associated with their commercial businesses – does not justify the burden Unregistered Members may have in identifying and retaining records of communications that lead to the execution of commodity interest

⁴¹ See AGA, MGEX, CEWG, CMC, IECA and ICI Comment Letters.

⁴² See 2012 Amendment Adopting Release at 75538.

and related cash or forward transactions. The Commission therefore has determined that Unregistered Members should not be required to keep records of written communications that lead to the execution of a commodity interest transaction and related cash or forward transactions. Instead, Unregistered Members will only be required to keep records of their transactions.

In addition to the comments addressed above, nine commenters representing a variety of commercial interests requested that Unregistered Members be excluded from the rule altogether.⁴³ Several commenters argued that the rule is simply too burdensome for Unregistered Members, particularly for Unregistered Members that are commercial end-users.⁴⁴ MGEX argued that the rule places a significant burden upon those Unregistered Members that are individuals that trade only for themselves, have purchased a membership for investment purposes, and/or only engage in low-risk commercial hedging. COPE and EEI stated that the Commission's recordkeeping rules relating to swaps and to large trader reporting already impose sufficient recordkeeping obligations on Unregistered Members, making compliance with Regulation 1.35(a) unnecessary. Multiple commenters asserted that the rule should only apply to intermediaries. Several commenters stated that the rule discourages Unregistered Members from membership on DCMs and SEFs. Finally, several commenters argued that there is no statutory basis for including Unregistered Members in the rule.⁴⁵

As far as Regulation 1.35(a) may present unique issues for Unregistered Members, the Commission is tailoring this Final Rule to accommodate those issues.

⁴³ See CMC, CEWG, COPE, EEG, FHLB, ICE, IECA, and NRECA & APPA Comment Letters.

⁴⁴ See CMC, IECA, MGEX, and NCFC Comment Letters.

⁴⁵ See CMC, IECA, and MGEX Comment Letters.

Specifically, Unregistered Members do not have to keep records of written communications that lead to the execution of a commodity interest transaction and related cash or forward transactions. They do not have to keep text messages and they do not have to maintain records in any particular form and manner. The Commission understands that Unregistered Members may wish to be excluded from Regulation 1.35(a) entirely. The Commission has already determined, however, that Unregistered Members are properly subject to the rule.⁴⁶ The policy reasons for this determination that were enunciated in 2012 continue to apply.⁴⁷ The recordkeeping requirements of Regulation 1.35(a), including those imposed on Unregistered Members, are an important component of the Commission's efforts to ensure fair, orderly and efficient markets, and to detect and deter abusive, disruptive, fraudulent, and manipulative acts that can harm market integrity and customers.⁴⁸

C. Proposal to Exclude Commodity Trading Advisors from the Requirement to Record and Maintain Oral Communications

Regulation 1.35(a) requires CTAs that are members of a DCM or of a SEF to record all oral communications that lead to the execution of a transaction in a commodity interest.⁴⁹ In considering the Proposed Amendment, the Commission noted that many CTAs who are members of a DCM or of a SEF have discretionary trading authority over customers' accounts and, therefore would not have routine telephone conversations with

⁴⁶ 2012 Amendment Adopting Release at 75525. The issues that commenters have raised regarding Unregistered Members, as summarized immediately above, are largely the same as the issues that were raised by commenters, and considered by the Commission, in 2012. Id. at 75527.

⁴⁷ Id. at 75528.

⁴⁸ Id.

⁴⁹ 17 CFR 1.35(a)(1).

customers that lead to the execution of a transaction in a commodity interest.⁵⁰ The Commission noted, however, that some CTAs may execute an order on behalf of a customer on a non-discretionary basis.⁵¹ The Commission stated that capturing customer orders was consistent with the regulatory goals of Regulation 1.35(a), although the costs of recording and keeping oral communications weighs against the benefit of achieving those goals.⁵² The Commission stated that the same was not true with respect to the costs of recording and maintaining written records, which the Commission understood to be significantly less than the costs of recording and maintaining oral communications.⁵³ Therefore, the Commission proposed to amend Regulation 1.35(a) to exclude CTAs from the requirement to record oral communications that lead to the execution of a transaction in a commodity interest.

In response to the Proposed Amendment and its effects on CTAs, the Commission received comments from representatives of five advisor and broker trade groups, one self-regulatory organization, and one exchange.⁵⁴ The commenters were supportive of this aspect of the Proposed Amendment, with most noting that CTAs and CPOs trade primarily on a discretionary basis, and therefore have little to no communication with customers regarding transactions. In addition, some commenters stated that CTAs are subject to extensive “analogous” recordkeeping requirements under Regulation 4.33 and SEC rules for investment advisers, which makes compliance with the oral recordkeeping

⁵⁰ See Proposal at 68143.

⁵¹ Id.

⁵² Id.

⁵³ Id.

⁵⁴ See IAA, ICI, MFA, SIFMA AMG, NIBA, NFA, and MGEX Comment Letters.

requirement of Regulation 1.35(a) unnecessary and unduly burdensome.⁵⁵ No commenters suggested that the Commission refrain from excusing CTAs from the requirement to record oral communications that lead to the execution of a transaction in a commodity interest.

Commenters also requested that the Commission provide CTAs with additional relief from the requirements of Regulation 1.35(a). IAA and ICI cited the reasons the Commission offered to exclude CTAs and CPOs from oral recordkeeping to argue that asset managers should be excluded from Regulation 1.35(a) entirely. For example, IAA and ICI stated that CTAs and CPOs act on a discretionary basis and have little to no communication with customers regarding orders. They also noted that any discussions CTAs and CPOs may have with market intermediaries regarding orders are captured by those intermediaries, making CTAs' and CPOs' records duplicative. Further, they noted that CTAs and CPOs are already subject to extensive recordkeeping rules under CFTC, SEC and state regulations. SIFMA AMG argued that the relief that the Commission staff provided to Unregistered Members, by excusing them from the requirements to retain text messages and to maintain other required records in a particular form and manner should be expanded to include all asset managers. SIFMA AMG stated that asset managers, including registered CTAs and CPOs, utilize text messages in a similar capacity as Unregistered Members. SIFMA AMG stated that the technology does not exist to maintain text messages pursuant to the rule. SIFMA AMG also argued that the costs associated with these recordkeeping obligations will "almost certainly" reduce the liquidity that asset managers provide to the swap markets. Further, as noted above,

⁵⁵ See IAA, ICI, MFA, and SIFMA AMG Comment Letters.

SIFMA AMG observed that asset managers are also subject to extensive regulation under other CFTC, SEC and state regulations.

The Commission has carefully considered commenters' requests that, in addition to the proposed relief from oral recordkeeping requirements, the Commission grant CTAs relief from the written recordkeeping requirements of Regulation 1.35(a). The Commission has stated in the past that access to searchable written records is an important tool the Commission needs to ensure market integrity and protect customers.⁵⁶ As some commenters have acknowledged, CTAs already maintain extensive written records that are analogous to those required by the rule.⁵⁷ The Commission's interest in ensuring customer protection and market integrity justifies the incremental costs to maintain these and other records pursuant to Regulation 1.35(a).

In response to SIFMA AMG's request to extend the relief granted to Unregistered Members to all asset managers, the Commission notes that asset managers are uniquely situated compared to Unregistered Members, in that asset managers may act as intermediaries.⁵⁸ As such, an asset manager's written records are more critical to the Commission's interest in promoting customer protection than those of Unregistered Members. The Commission nonetheless recognizes the burdens that CTAs face when complying with Regulation 1.35(a), and has alleviated some of that burden by excluding them entirely from the oral recordkeeping requirements of the rule. Therefore, the Commission is adopting the Final Rule as proposed.

⁵⁶ See 2012 Amendment Adopting Release at 75528.

⁵⁷ See IAA, ICI, MFA, and SIFMA AMG Comment Letters.

⁵⁸ CFTC Staff Letter No. 14-72 granted relief to Unregistered Members from the requirements to retain text messages and to maintain records in a particular form and manner. The Proposal sought to codify that relief.

D. Reorganization of Paragraph (a) of Commission Regulation 1.35

The final rule text of paragraph (a) of Commission Regulation 1.35 as adopted in this release has been reorganized to provide greater clarity regarding the regulatory obligations of affected Commission registrants and Unregistered Members. To this end, the reorganized rule text defines separate categories of required records and then separately specifies for each type of Commission registrant, and for Unregistered Members, the category or categories of records each is required to keep. For the avoidance of doubt, other than as modified by the amendments to paragraph (a) of Commission Regulation 1.35 that the Commission is adopting in this release, the Commission reiterates that the text of paragraph (a) has only been reorganized; the reorganized rule text is not intended to modify the regulatory obligations of Commission registrants or Unregistered Members under Commission Regulation 1.35(a) in any other respect.

IV. Related Matters

A. Regulatory Flexibility Act

The Regulatory Flexibility Act requires that Federal agencies consider whether the rules they propose will have a significant economic impact on a substantial number of small entities and, if so, they must provide a regulatory flexibility analysis respecting the impact.⁵⁹ Whenever an agency publishes a general notice of proposed rulemaking for any rule, pursuant to the notice-and-comment provisions of the Administrative Procedure Act⁶⁰ a regulatory flexibility analysis or certification typically is required.⁶¹ The

⁵⁹ 5 U.S.C. 601 et seq.

⁶⁰ 5 U.S.C. 553. The Administrative Procedure Act is found at 5 U.S.C. 500 et seq.

⁶¹ See 5 U.S.C. 601(2), 603–05.

Commission stated in the Proposal that, if adopted, the Proposal would not have a significant economic impact on affected entities because it would relieve them from certain regulatory obligations that would otherwise apply to them. Specifically, the Final Rule provides relief from certain recordkeeping requirements in Regulation 1.35(a), and the Final Rule does not impose any new regulatory obligations on affected persons. Commenters agreed that the Proposal would decrease regulatory burdens on certain market participants. No commenter stated that the Proposal would impose any new regulatory obligations on affected persons.

Accordingly, the Chairman, on behalf of the Commission, hereby certifies pursuant to 5 U.S.C. 605(b) that the rule amendment adopted herein will not have a significant economic impact on a substantial number of small entities.⁶²

B. Paperwork Reduction Act

As the Commission stated in the Proposal, this rulemaking does not impose any new recordkeeping or information collection requirements, or other collections of information that require approval of the Office of Management and Budget under the Paperwork Reduction Act (“PRA”). All recordkeeping or information collection requirements relevant to the subject of this rulemaking, or discussed herein, already exist under current law. The title for this collection of information is “Adaptation of Regulations to Incorporate Swaps—Records of Transactions,” OMB control number 3038-0090. The Commission invited public comment on the accuracy of its estimate that no additional recordkeeping or information collection requirements or changes to existing collection requirements would result from the Proposed Amendment. The Commission

⁶² The Chairman made the same certification in the Proposed Amendment.

did not receive any comments that addressed whether additional recordkeeping or information collection requirements or changes to existing collection requirements would result from the adoption of the Proposal. Nevertheless, the Commission notes that the final rule will reduce the current burden of OMB control number 3038-0090.

Accordingly, the Commission will, by separate action, publish in the Federal Register a notice and request for comment on the amended PRA burden associated with the final rule, and submit to OMB an information collection request to amend the information collection, in accordance with 44 U.S.C. 3506(c)(2)(A) and 5 CFR 1320.8(d).

C. Cost-Benefit Considerations

Section 15(a) of the CEA requires the Commission to consider the costs and benefits of its actions before promulgating a regulation under the CEA or issuing certain orders. Section 15(a) further specifies that the costs and benefits shall be evaluated in light of five broad areas of market and public concern: (1) protection of market participants and the public; (2) efficiency, competitiveness, and financial integrity of futures markets; (3) price discovery; (4) sound risk management practices; and (5) other public interest considerations. In adopting the Final Rule, the Commission has considered the costs and benefits resulting from its discretionary determinations with respect to the Section 15(a) factors, and sought comments from interested persons regarding the nature and extent of such costs and benefits.

In summary, as the Commission stated in the 2012 Amendment, the records (as well as the form and manner in which such records must be kept) under Regulation 1.35 are an important component of the Commission's efforts to ensure fair, orderly and efficient markets, and to detect and deter abusive, fraudulent and manipulative acts and

practices that can harm market integrity and customers. In furthering the important policy and practical objectives of the rule, the Commission carefully considered the potential impact on the market and market participants. The adoption of the Final Rule reflects the agency's efforts to consider the need to promote market integrity and protect customers, while mitigating potential cost to market participants, and in particular, commercial end-users.

1. Background

The Commission is amending Regulation 1.35(a) to: (i) provide that all records that are required to be maintained under this regulation must be maintained in a form and manner which permits prompt, accurate and reliable location, access, and retrieval of any particular record, data, or information; (ii) clarify that the requirement that records be kept in a form and manner identifiable by transaction means that the records must be kept in a form and manner that allows for identification of a particular transaction, except that records of oral and written communications leading to the execution of a commodity interest transaction and related cash or forward transactions are not required to be kept in a form and manner that allows for identification of a particular transaction; (iii) exclude Unregistered Members of DCMs and of SEFs from the requirements to: keep written communications that lead to the execution of a commodity interest transaction and related cash or forward transactions; keep text messages; and keep records in a particular form and manner; and (iv) exclude commodity trading advisors CTAs from the oral recordkeeping requirement. The Commission stated in the Proposal that the baseline for this cost and benefit consideration is the existing Regulation 1.35(a). While CFTC Staff Letters 14-72 and 14-147, as discussed above, currently provide no-action relief that is

substantially similar to much of the relief the Final Rule provides to certain Commission registrants and Unregistered Members, the Commission believes that CFTC Staff Letters 14-72 and 14-147 should not set or affect the baseline from which the Commission considered the costs and benefits of the Final Rule. This is because, as they indicate, CFTC Staff Letters 14-72 and 14-147 do not necessarily represent the position or view of the Commission or any other office or division of the Commission.

The Commission invited comments from the public on all aspects of its preliminary consideration of the costs and benefits associated with the Proposal, and the Cost-Benefit Considerations section of the Proposal included specific questions regarding certain aspects of potential costs or potential benefits associated with the Proposal. While those who commented on the Proposal generally did not specifically address the Cost-Benefit Considerations section of the Proposal, certain of the comments raised issues that relate to the Commission's cost-benefit considerations. Accordingly, although the Commission has addressed those comments above in connection with the specific proposed regulatory provision of the Proposal to which they referred, the Commission is also addressing those comments in the discussion that follows.

2. Costs.

The Commission stated in the Proposal that it would not impose any new or additional costs directly upon affected market participants, but instead would reduce some of the regulatory burdens and associated costs that Regulation 1.35(a) imposes upon them. The Commission stated that it is difficult to quantify what costs, if any, the Proposed Amendment would impose upon other market participants, the markets themselves, or the general public. The Commission observed, however, that one possible

cost associated with the Proposed Amendment would be that certain market participants, such as CTAs that are members of a DCM or of a SEF and Unregistered Members, would no longer be required to keep certain types of records that may be useful for the Commission in exercising its oversight of the markets, including for market surveillance, enforcement, and ensuring market integrity. The Commission invited public comments on the costs of the Proposal.

No commenter attempted to quantify the costs, if any, associated with the Proposal. Two commenters specifically stated that the Proposal would not affect market oversight.⁶³ Additionally, some commenters representing advisor trade groups noted that CTAs and CPOs are subject to extensive recordkeeping obligations under other CFTC, SEC and state regulations that are substantially similar to the requirements of Regulation 1.35(a). Therefore, the commenters that addressed this issue agreed that the Proposal would not significantly impact the Commission's ability to oversee the markets. The majority of commenters stated that the Proposal would reduce the regulatory burdens and costs associated with Regulation 1.35(a).

Many commenters argued, however, that the Proposal should have provided additional relief to Unregistered Members, especially those Unregistered Members that are commercial end-users. These commenters argued that this lack of additional relief would cause some end-users to avoid membership on DCMs and SEFs, resulting in increased transaction costs for those entities. These commenters also argued that such additional costs may cause market participants to conduct some swap transactions away from SEFs, which would, in turn, decrease market transparency and the Commission's

⁶³ CEWG and IECA Comment Letters.

ability to oversee the markets. As explained above, in adopting the Final Rule that provides additional relief to Unregistered Members, the Commission has attempted to address some of the concerns raised by end-users, which in turn should mitigate the impact of the rule on the broader market.

Finally, Voitrax commented that the Commission's changes to an existing rule may create a disincentive for some firms to develop technology to address Commission rules. Any rule amendment may have some effect on market participants, as well as the vendors that support those market participants. In this case, the Commission has tailored the rule to address some concerns that market participants have presented in a manner consistent with the overall purpose of the rule. However, the Commission believes that the Final Rule preserves the core market integrity and customer protection aspects of the rule, while reducing the recordkeeping obligations imposed by the rule.⁶⁴ The Commission therefore believes the costs associated with the Final Rule, to the extent that such costs exist, are negligible.

3. Benefits

The Commission stated in the Proposal that it would have a direct and tangible benefit for those market participants that are excused from certain aspects of the recordkeeping obligations of Regulation 1.35(a). The Commission reduced the burden of Regulation 1.35(a) by excluding CTAs and Unregistered Members from certain aspects of the rule. The Commission replaced the requirement that records be searchable by transaction with the more general requirement that records be searchable. The Commission observed that it may be difficult to quantify what other benefits the Proposal

⁶⁴ The Commission notes that the technology described in Voitrax's Comment Letter may still be useful in helping market participants comply with the form and manner requirements prescribed in the Final Rule.

may have for other market participants, the markets themselves, or the general public. The Commission invited public comments on the benefits of the Proposal. In response to those comments, the Commission is further reducing the burden of Regulation 1.35(a) by replacing the term “searchable” that was in the Proposal with the phrase “maintained in a form and manner which permits prompt, accurate and reliable location, access, and retrieval of any particular record, data, or information.” No commenters attempted to quantify the benefits associated with the Proposal. Commenters generally agreed that the Proposal would reduce recordkeeping costs for certain market participants. The Commission believes the benefits associated with the Final Rule, which are difficult to quantify in the aggregate, will be realized in different ways by different market participants affected by the rule depending on the precise nature of their business and the attendant recordkeeping obligations that accompany that business.

4. Section 15(a)

Section 15(a) of the CEA requires the Commission to consider the effects of its actions in light of the following five factors:

a. Protection of Market Participants and the Public

The Commission stated in the Proposal that it would reduce some of the regulatory burdens on certain market participants. The Commission recognizes that there may be a trade-off between reducing regulatory burdens and ensuring that the recordkeeping obligations Rule 1.35(a) imposes upon those market participants subject to the rule are sufficient to support the effort by the Commission to fulfill its regulatory mission. As noted above, the Proposal would relieve certain market participants from the requirement under Regulation 1.35(a) to keep certain types of records that can be

useful for the Commission in exercising its oversight of the markets, including for market surveillance, enforcement, and ensuring market integrity. The Commission invited public comment on these issues.

No commenter stated that the Proposal would adversely affect the ability of the Commission to provide effective oversight of the markets. Two commenters specifically stated that the Proposal would not affect market oversight.⁶⁵ Additionally, some commenters representing advisor trade groups noted that CTAs and CPOs are subject to extensive recordkeeping obligations under other CFTC, SEC and state regulations that are substantially similar to the requirements of Regulation 1.35(a). Therefore, the commenters that addressed this issue agreed that the Proposal would not significantly impact the Commission's ability to oversee the markets. The Commission agrees with commenters that its access to records will remain sufficient to protect market participants and the public.

Some commenters argued that that the Proposal did not go far enough in relieving burdens on commercial end-users, which they argue creates a disincentive to transact on DCMs and SEFs, thereby lowering market transparency. As explained above, in adopting the Final Rule that provides additional relief to Unregistered Members, the Commission has attempted to address some of the concerns raised by end-users, which in turn should mitigate the impact of the rule on the broader market.

b. Efficiency, Competitiveness, and Integrity of Markets

The Amendments to Rule 1.35(a) are intended, in part, to reduce some of the regulatory burdens on certain market participants and end-users. The Commission

⁶⁵ CEWG and IECA Comment Letters.

invited public comment on whether the Proposed Amendment, if adopted, would actually decrease these regulatory burdens, and whether the decreased regulatory burdens would result in increased resource-allocation efficiency and competition without compromising market integrity.

Commenters generally stated that the Proposal would decrease the regulatory burdens on affected market participants. No commenters addressed whether the relief provided in the Proposed Amendment would result in increased efficiency and competition among market participants. No commenter stated that the Proposal would compromise market integrity. In fact, no commenters addressed whether the Proposal would affect market integrity.

The Commission believes that the Final Rule will decrease the regulatory burdens on affected market participants. The Commission believes that this should result in increased resource-allocation efficiency for market participants overall. The Commission believes that the Final Rule should not have any effect on competition. Finally, the Commission believes that the Final Rule will not compromise market integrity. The Final Rule is narrowly tailored to provide relief to certain market participants with respect to certain types of records. This targeted relief does not unduly compromise the recordkeeping requirements of Regulation 1.35(a), the CEA, or other Commission Regulations.

Some commenters stated that the lack of sufficient relief provided in the Proposed Amendment would cause many market participants to avoid utilizing SEFs. Further, one commenter stated that costs associated with these recordkeeping obligations will “almost certainly” reduce the liquidity that asset managers provide to the swap markets. Many

commenters agreed that although the Proposal decreased the regulatory burdens on Unregistered Members, it did not go far enough, resulting in decreased resource-allocation efficiency of the markets. As explained above, in adopting the Final Rule that provides additional relief to Unregistered Members, the Commission has attempted to address some of the concerns raised by end-users, which in turn should mitigate the impact of the rule on the broader market.

c. Price Discovery

The Commission stated that the Proposed Amendment would not have any effect on price discovery. The Commission invited public comments regarding what effect, if any, the Proposed Amendment would have on price discovery. Only one commenter addressed price discovery, stating that the Proposal would not have any effect on price discovery.⁶⁶ The Commission has no basis to believe that the Final Rule will have any effect on price discovery.

d. Sound Risk Management

The Proposal is intended, in part, to reduce some of the regulatory burdens on certain market participants. The Commission invited public comment on whether the Proposed Amendment would have any effect on the risk management practices of market participants and end-users. Commenters agreed that the Proposed Amendment would, if adopted, decrease regulatory burdens on certain market participants. Commenters did not address whether these decreased regulatory burdens would have an effect on market participants' risk management practices. One commenter stated that the Proposed Amendment did not provide sufficient relief to Unregistered Members that are

⁶⁶ IECA Comment Letter.

commercial end-users, which they assert perpetuates a disincentive for these firms to transact on SEFs.⁶⁷ The commenter argues that any disincentive to SEF utilization decreases the risk management options that are available to Unregistered Members. As explained above, in adopting the Final Rule that provides additional relief to Unregistered Members, the Commission has attempted to address some of the concerns raised by end-users, which in turn should mitigate the impact of the rule on the broader market.

e. Other Public Interest Considerations

The Commission did not identify any other public interest considerations for this rulemaking, nor were any identified by commenters.

List of Subjects in 17 CFR Part 1

Agricultural commodity, Agriculture, Brokers, Committees, Commodity futures, Conflicts of interest, Consumer protection, Definitions, Designated contract markets, Directors, Major swap participants, Minimum financial requirements for intermediaries, Reporting and recordkeeping requirements, Swap dealers, Swaps.

For the reasons stated in the preamble, the Commodity Futures Trading Commission amends 17 CFR part 1 as set forth below:

PART 1 – GENERAL REGULATIONS UNDER THE COMMODITY EXCHANGE ACT

1. The authority citation for part 1 continues to read as follows:

Authority: 7 U.S.C. 1a, 2, 5, 6, 6a, 6b, 6c, 6d, 6e, 6f, 6g, 6h, 6i, 6k, 6l, 6m, 6n, 6o, 6p, 6r, 6s, 7, 7a-1, 7a-2, 7b, 7b-3, 8, 9, 10a, 12, 12a, 12c, 13a, 13a-1, 16, 16a, 19, 21, 23, and 24 (2012).

⁶⁷ IECA Comment Letter.

2. In § 1.35, revise paragraphs (a)(1) through (4) and add paragraphs (a)(5) through (9) to read as follows:

§ 1.35 Records of commodity interest and related cash or forward transactions.

(a) * * *

(1) Futures commission merchants, retail foreign exchange dealers, and certain introducing brokers. Each futures commission merchant, retail foreign exchange dealer, and introducing broker that has generated over the preceding three years more than \$5 million in aggregate gross revenues from its activities as an introducing broker, shall:

(i) Keep full, complete, and systematic records (including all pertinent data and memoranda) of all transactions relating to its business of dealing in commodity interests and related cash or forward transactions, which shall include all orders (filled, unfilled, or canceled), trading cards, signature cards, street books, journals, ledgers, canceled checks, copies of confirmations, copies of statements of purchase and sale, and all other records, which have been prepared in the course of its business of dealing in commodity interests and related cash or forward transactions (for purposes of this section, all records described in this paragraph (a)(1)(i) are referred to as “commodity interest and related records”);

(ii) If such person is a member of a designated contract market or swap execution facility, retain and produce for inspection all documents on which trade information is originally recorded, whether or not such documents must be prepared pursuant to the rules or regulations of either the Commission, the designated contract market or the swap execution facility (for purposes of this section, all records described in this paragraph

(a)(1)(ii) are referred to as “original source documents,” and, together with commodity interest and related records, “transaction records”); and

(iii) Keep 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 any related cash or forward transactions (but not oral communications that lead solely to the execution of a related cash or forward transaction), whether transmitted by telephone, voicemail, facsimile, instant messaging, chat rooms, electronic mail, mobile device, or other digital or electronic media (for purposes of this section, all communications described in this paragraph (a)(1)(iii) are referred to as “oral pre-trade communications” if transmitted orally or as “written pre-trade communications” if transmitted in writing, and all such communications are referred to collectively as “pre-trade communications”).

(2) Registered members of designated contract markets or swap execution facilities. Each introducing broker that is not subject to paragraph (a)(1) of this section and is a member of a designated contract market or swap execution facility, and each member of a designated contract market or swap execution facility that is registered or required to be registered with the Commission as a floor trader, commodity pool operator, commodity trading advisor, swap dealer, or major swap participant, shall keep:

- (i) All transaction records; and
- (ii) All written pre-trade communications.

(3) Other introducing brokers. Each introducing broker that is not subject to paragraph (a)(1) or (2) of this section shall keep:

- (i) All commodity interest and related records; and

(ii) All written pre-trade communications.

(4) Floor broker members of designated contract markets or swap execution facilities. Each member of a designated contract market or swap execution facility that is registered or required to be registered with the Commission as a floor broker shall keep:

(i) All transaction records;

(ii) All written pre-trade communications; and

(iii) All oral pre-trade communications that lead to the purchase or sale of any commodity for future delivery, security futures product, swap, or commodity option authorized under section 4c of the Commodity Exchange Act for the account of any person other than such floor broker.

(5) Form and manner. All records required to be kept pursuant to paragraphs (a)(1), (2), (3), and (4) of this section shall be kept in a form and manner that:

(i) Permits prompt, accurate, and reliable location, access, and retrieval of any particular record, data, or information; and

(ii) Other than pre-trade communications, allows for identification of a particular transaction.

(6) Unregistered members of designated contract markets or swap execution facilities. Each member of a designated contract market or swap execution facility that is not registered or required to be registered with the Commission in any capacity, shall keep all transaction records; provided that such records need not include transmissions by short message service (SMS) or multimedia messaging service (MMS).

(7) Definition of related cash or forward transaction. For purposes of this section, “related cash or forward transaction” means a purchase or sale for immediate or deferred

physical shipment or delivery of an asset related to a commodity interest transaction where the commodity interest transaction and the related cash or forward transaction are used to hedge, mitigate the risk of, or offset one another.

(8) Other requirements. Each futures commission merchant, retail foreign exchange dealer, introducing broker, and member of a designated contract market or swap execution facility shall retain the records required to be kept by this section in accordance with the requirements of § 1.31, and produce them for inspection and furnish true and correct information and reports as to the contents or the meaning thereof, when and as requested by an authorized representative of the Commission or the United States Department of Justice.

(9) Alternative Compliance Schedule. (i) The Commission may in its discretion establish an alternative compliance schedule for the requirement to record oral communications under paragraph (a)(1) or (4) of this section that is found to be technologically or economically impracticable for an affected entity that seeks, in good faith, to comply with the requirement to record oral communications under paragraph (a)(1) or (4) of this section within a reasonable time period beyond the date on which compliance by such affected entity is otherwise required.

(ii) A request for an alternative compliance schedule under paragraph (a)(9)(i) of this section shall be acted upon within 30 days from the time such a request is received, or it shall be deemed approved.

(iii) The Commission hereby delegates to the Director of the Division of Swap Dealer and Intermediary Oversight or such other employee or employees as the Director may designate from time to time, the authority to exercise the discretion.

Notwithstanding such delegation, in any case in which a Commission employee delegated authority under this paragraph believes it appropriate, he or she may submit to the Commission for its consideration the question of whether an alternative compliance schedule should be established. The delegation of authority in this paragraph shall not prohibit the Commission, at its election, from exercising the authority set forth in paragraph (a)(9)(i) of this section.

(iv) Relief granted under paragraph (a)(9)(i) of this section shall not cause an affected entity to be out of compliance or deemed in violation of any recordkeeping requirements.

* * * * *

Issued in Washington, DC, on December 18, 2015, by the Commission.

Christopher J. Kirkpatrick,
Secretary of the Commission.

NOTE: The following appendices will not appear in the Code of Federal Regulations.

**Appendices to Records of Commodity Interest and Related Cash or Forward
Transactions – Commission Voting Summary, Chairman’s Statement, and
Commissioner’s Statement**

Appendix 1 – Commission Voting Summary

On this matter, Chairman Massad and Commissioners Bowen and Giancarlo voted in the affirmative. No Commissioner voted in the negative.

Appendix 2 – Statement of Chairman Timothy G. Massad

Today, the Commission is adopting significant changes to a rule that will reduce recordkeeping obligations for commercial end-users. The changes ensure that the rule strikes an appropriate balance between the costs of recordkeeping and the benefits to market oversight. This will help ensure that businesses as well as farmers and ranchers that depend on the derivatives markets are able to continue using them effectively and efficiently.

Commercial end-users were not the cause of the crisis, and should not bear the burdens of reforms designed to rein in systemic risk. Since I became Chairman, the CFTC has taken a number of actions to fine-tune our rules to ensure they do not impose unintended burdens on those who use the derivatives markets to hedge commercial risk. Today, I'm pleased to support another final rule that makes important strides towards that goal.

This final rule amends recordkeeping requirements set forth under Commission Regulation 1.35. This regulation requires various types of market participants to keep written and oral records of their commodity interest and related cash or forward transactions. It is very important to our efforts to ensure our markets are strong, transparent, and operate free of fraud and manipulation.

This rule was first implemented in 1948. CFTC made changes to this regulation in 2012, to ensure it accurately reflected evolution of the market and changes in the CFTC's jurisdiction. But we have been evaluating the rule since then, and we have determined that for some market participants, the costs of complying with certain aspects of the changes may exceed the potential benefits. Throughout this process, we have

benefitted from the input of many commercial businesses and other market participants. We appreciate their feedback.

Today's final rule clarifies that members of exchanges and swap execution facilities not registered with the Commission—typically, end-users—do not have to keep pre-trade communications or text messages. Further, it simplifies the requirements for keeping records of final transactions. The amended rule also states that commodity trading advisors do not have to record oral communications regarding their transactions.

I believe this rule is an important change that will reduce recordkeeping burdens on end-users, and I applaud my fellow commissioners for their unanimous support.

Appendix 3 – Statement of Commissioner J. Christopher Giancarlo

I am pleased to support this final rule that revises Rule 1.35. In the end, after numerous iterations, several comment periods, significant legislative interest from Congress, and months of negotiating, the Commodity Futures Trading Commission (“CFTC” or “Commission”) thankfully listened to the concerns of market participants. I am appreciative of the CFTC staff's diligent work over the past few months to make key revisions to this rule. Fixing this regulation was one of the first issues that I raised with my fellow Commissioners upon my arrival at the CFTC. I believe we have now produced a more workable rule that will not impose needless regulatory costs on America's agricultural producers, grain elevator operators or energy producers, to name a few.

As background, the Commission revised long-standing Rule 1.35 in 2012 despite the fact that the Dodd-Frank Act¹ contained no mandate to change the CFTC's recordkeeping rules.² The revised rule proved to be unworkable. Its publication was followed by requests for no-action relief and a public roundtable at which entities impacted by the rule voiced their inability to tie all communications leading to the execution of a transaction to a particular transaction or transactions. End-user exchange members pointed out that business that was once conducted by telephone had moved to text messaging, so the carve out in the rule for oral communications had little utility. They pointed out that it was simply not technologically feasible to keep pre-trade text messages in a form and manner "identifiable and searchable by transaction." Further, bipartisan Congressional action on the rule's unworkable nature made it clear that the Commission should re-open the rule to lessen the burden on market participants not registered with the CFTC.³

In November 2014, the CFTC did propose changes to Rule 1.35.⁴ Unfortunately, I could not support that proposal because it did not go far enough in addressing concerns about the feasibility and cost of compliance.⁵ It continued to contain provisions that were overly burdensome in practice for certain covered entities. For example, the proposal kept 2012 rule revisions that required the keeping of all oral and written records that lead

¹ Dodd-Frank Wall Street Reform and Consumer Protection Act, Public Law 111-203, 124 Stat. 1376 (2010).

² See Adaptation of Regulations to Incorporate Swaps-Records of Transactions, 77 FR 75523 (Dec. 21, 2012), available at <https://www.gpo.gov/fdsys/pkg/FR-2012-12-21/pdf/2012-30691.pdf>.

³ See H.R. 4413, the Customer Protection and End-User Relief Act, Sec. 353 (113th Congress) and H.R. 2289, the Commodity End-User Relief Act, Sec. 308 (114th Congress).

⁴ See Records of Commodity Interest and Related Cash or Forward Transactions, 79 FR 68140 (Nov. 14, 2014), available at <http://www.cftc.gov/idc/groups/public/@lrfederalregister/documents/file/2014-26983a.pdf>.

⁵ See *id.* at 68147-148 (Dissenting Statement of Commissioner J. Christopher Giancarlo).

to the execution of a transaction in a commodity interest and related cash or forward transaction, in a form and manner “identifiable and searchable by transaction.”⁶ This “searchable” requirement also conflicted with the requirements of Commission Rule 1.31, which applies to all books and records required to be kept by the Commodity Exchange Act and Commission regulations.

Appropriately, the final revisions to Rule 1.35 address many of the issues raised in my year-old dissent. End-user exchange members that are not registered or required to be registered with the Commission now must only keep transaction records, which is a logical and prudent course of regulatory policy. Text messages are also excluded from the recordkeeping requirement for end-users, but communications through internet-based messaging services must be kept on file. I anticipate that this distinction will generate interesting public commentary.⁷

Aside from the technical points of the final rule, it is appropriate to comment on the skyrocketing compliance costs associated with trading in American commodity markets. There is an undeniable need for the CFTC to police these markets and root out fraud and abuse. Confidence and trust in our markets is essential so that farmers, manufacturers and other end-users can safely hedge their risks and costs of production. Yet, agricultural intermediaries, particularly small futures commission merchants, are being squeezed by the prolonged environment of low interest rates and increased regulatory burdens. Regulators must always balance the public’s interest in collecting

⁶ See *supra* note 4.

⁷ As finalized, the rule excludes text messages based on SMS and MMS technology, but includes internet-based messaging services such as iPhone messages because they are easier to store and retrieve on computers. While this outcome is puzzling and not technologically neutral, the best manner to ensure compliance with CFTC regulations is education on our rules.

commercial information for use in investigations and enforcement, against costs and burdens placed on American commerce and industry and the jobs they generate. In this protracted period of weak economic growth with an enormous number of Americans out of the workforce, we must scrupulously avoid needless red tape and compliance costs that are invariably passed along through higher costs for everyday items like a loaf of bread or a gallon of gasoline, milk or winter heating oil.

I believe the final Rule 1.35 generally gets the balance right. Yet, I must give a plain and simple warning: The elimination of unnecessary recordkeeping burdens provided in this final rule will be paradoxically tossed aside for many small market participants if Regulation Automated Trading (“Regulation AT”) is finalized as proposed.⁸ Under Regulation AT, many unregistered market participants would be forced to register for the first time with the CFTC as “floor traders” due to the broad definition of “algorithmic trading.”⁹ As new floor traders, these market participants would then be subject to heightened recordkeeping requirements under Rule 1.35, such as keeping all “written communications provided or received concerning quotes, bids, offers, instructions, trading, and prices that lead to the execution of a transaction.”¹⁰ As I said in my statement accompanying the Notice of Proposed Rulemaking for Regulation AT, I encourage market participants to carefully review and consider the compliance and

⁸ See CFTC Notice of Proposed Rulemaking (3038-AD52), Regulation Automated Trading (Dec. 14, 2015), available at <http://www.cftc.gov/idx/groups/public/@newsroom/documents/file/federalregister112415.pdf>.

⁹ See definition of “Algorithmic Trading” in proposed Commission regulation 1.3(zzzz), which is very broad and would appear to capture market participants using off-the-shelf type automated systems or simple excel spreadsheets to automate trading.

¹⁰ Emphasis added; see Commission Rule 1.35(a)(1)(iii) (defining “written pre-trade communications”) and Rule 1.35(a)(2)(ii) (requiring all “floor traders” to keep all “written pre-trade communications”).

cost consequences of that potential new regulatory regime and compare it to today's common-sense revisions to Rule 1.35.

As I have mentioned in the past, I have been fortunate during my time as a Commissioner to visit with agricultural and energy producers and intermediaries in Illinois, Indiana, Iowa, Minnesota, Texas, Louisiana and Kentucky. The common refrain I hear again and again is that Washington does not listen to everyday Americans. It imposes rules and regulations without regard to their obvious impact on ordinary people. Well, I believe this rule benefits from listening to those concerns and is a step in the right direction. I am hopeful that it is an indicator of future action by the CFTC that more readily takes to heart these common concerns in all of our regulatory actions.

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