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Regulations Regarding Derivatives Transaction Facilities (DTF)

New CFTC Part 37 as Applied to Commercials

Scope of DTF

- A contract, agreement, or transaction traded on a multilateral transaction execution facility,* the facility, and the facility's operator are exempt from all provisions of the Commodity Exchange Act (CEA) and from all Commodities Future Trading Commission (CFTC or Commission) regulations under the CEA except those enumerated in Rule 37.5(a),** if (Rule 37.2):

* Multilateral transaction execution facility (MTEF) means a market or similar facility through which persons agree to enter into or execute binding transactions by accepting bids or offers made by one person that are open to multiple persons who conduct business through such market or similar facility, but does not include: (i) a facility which allows participants to individually negotiate the material terms of the transactions, (ii) an electronic communication which produces transactions based solely on bilateral communication between the parties rather than the automated interaction of multiple orders, or (iii) any facility which allows only one firm to act as a market maker and other participants may not accept bids or offers of other non-market makers. (Rule 36.1(b))

** Sections 1a, 2(a)(1), 4, 4b, 4c, 4g, 4i, 4o, 5(6), 5(7), the rule disapproval procedures of 5a(a)(12), 5b, 6(a), 6(b), 6(c), 6b, 6c, 8(a), 8(c), 8a(6), 8a(7), 8a(9), 8c(a), 9(a)(2), 9(a)(3), 9(f), 14, 20, and 22 of the CEA and Rules 1.3, 1.31, 1.37, 1.41, 5.3, 33.10, Part 5, Part 20, and Part 37 of Title 17 Chapter 1 of the CFR continue to apply. (See "Sections of the CEA and Rules which apply to DTFs" (pp. 9-17) for how these provisions may impact DTFs).

- ▶ Only eligible commercial participants* trading for their own account have trading access to the DTF for contracts, agreements or transactions in any commodity except those listed in section 1(a)(3) of the CEA (agricultural commodities);
- ▶ The MTEF must be recognized as a DTF by the Commission (Rule 37.2(b));
- ▶ The MTEF must comply with all the conditions of the DTF exemption (Part 37) and must disclose to participants transacting on or through its facility that these transactions are subject to the provisions of Part 37 (Rule 37.2(c));
- ▶ If cleared, the submission of contracts, agreement, or transactions for clearance or settlement must be through a clearinghouse authorized by the Commission (Rule 37.2(d)); and
- ▶ The products traded by an electronic system must be clearly identified as traded on a recognized derivatives transaction facility or if traded in a physical trading environment must be traded in a location separate from products traded as designated contracts markets (Rule 37.2(e)).

* Eligible Commercial Participant means and shall be limited to a party that is either: (i) a bank or trust company (acting on its own behalf or another eligible participant), (ii) a savings association or credit union, an insurance company, (iii) a corporation, partnership, proprietorship, organization, trust, or other entity not formed solely for the purpose of being an eligible participant, and the entity has a (A) total assets exceeding \$10,000,000, or (B) has a letter or credit guaranteeing the obligations of the entity under the agreement or (C) has a net worth of \$1,000,000 and enters the agreement in connection with the conduct its business or to manage the risk of one of its assets, and (iv) any governmental or multinational entity. In order to qualify, the entity must, in connection with its business, make and take delivery of the underlying physical commodity and regularly incur risks related to such commodity. Dealers that regularly provide hedging, risk management, or market-making services to Eligible Commercial Participants are also considered Eligible Commercial Participants.

Conditions for Recognition as a DTF

- In order to be recognized as a DTF, a facility must initially have:
 - ▶ Rules for trading on its facility including, depending on the nature of the trading mechanism (Rule 37.3(a)(1)):
 - ◆ Rules to deter trading abuse, adequate power and capacity to detect, investigate, and take actions against violations of its rules; or
 - ◆ Use of technology that provides participants in the facility with impartial access to transactions and retains information necessary to document violations or rules.
 - ◆ Rules defining the operation of the trading mechanism for the facility or the electronic matching platform. (Rule 37.3(a)(2)).
- A DTF must initially and on a continuing basis follow seven core principles (Rule 37.3(b)):
 - ▶ Enforcement: Monitor and enforce its own rules, including rules on access, if such rules exist.
 - ▶ Market Oversight: As appropriate, the DTF should monitor markets to ensure orderly trading and an orderly market, or alternatively provide to the CFTC any information requested to satisfy the DTF's obligations under the CEA.
 - ▶ Operational Information: Disclose to regulators and market participants, to the extent possible, information concerning trading terms, contract terms and conditions, trading mechanisms, financial integrity arrangements or mechanisms, as well as other relevant information.
 - ▶ Transparency: Provide market participants equal access to information regarding prices, bids and offers, and other relevant information to the market. Inform the public of price and trading information of "actively traded products." The level of trading necessary for a commodity to be an actively traded product is not defined by the new rule.
 - ▶ Fitness: Have fitness standards for members, operators or owners with greater than 10 percent interest or an affiliate of such an owner, member of the governing board, and individuals who make disciplinary determinations

- ▶ Record Keeping: Keep full books and records of all activities related to its business as a DTF, including information to reconstruct all trading for five years in a form acceptable to the Commission. Keep books and records readily available for two years.
- ▶ Competition: Avoid unreasonable restraints of trade or imposing any burden not necessary or appropriate in furtherance of the objections of the Act or the regulations thereunder.

Methods for Recognition as a DTF

- ▶ Any entity shall be recognized by the CFTC as a DTF thirty days after the Commission receives its application as long as (Rule 37.4(b)):
 - ▶ The application demonstrates the entity satisfies the conditions for recognition as a DTF, as detailed above;
 - ▶ The submission specifies it is being submitted pursuant to Part 37;
 - ▶ The submission includes a copy of the DTF's rules and a brief of explanation of how those rules satisfies each of the conditions for recognition under Rule 37.3 (See "Conditions for Recognition as a DTF" on p. 3);
 - ▶ The applicant does not amend its application during the 30-day period except for typographical errors or at the request of the CFTC; and
 - ▶ The applicant has not instructed the CFTC to review the application under Section 6 of the CEA. Section 6 is the standard review process for a board of trade to be designated as a contract market. A board of trade must show it complies with and assure that it will continue to comply with Section 5 of the CEA. The Commission may review an application under Section 6 for up to one year before approving or disapproving the application. If the Commission notifies a board of trade that its application is complete, the one year time period for approval shall be stayed until a complete application is submitted. However, the Commission shall approve or deny any application resubmitted in complete form within sixty days of resubmission.
- If the CFTC determines that the applications fails to meet the conditions for recognition as a DTF, it will terminate the review period and give notice of the issues raised and faults within the application. The applicant can within 10 days request a final ruling on the application under Section 6 of the CEA (Rule 37.3(c)).

Approval of Rule Changes

- All rules changes must be submitted for approval except (Rules 37.4(e), 1.41(c)(2)):
 - ▶ DTFs may place a rule into effect without prior Commission review or approval if the DTF files with the Commission a submission labeled "DTF Rule Notice" that includes the text of the rule or the amendment at the time traders or participants in the market are notified, but it must be filed by the close of business on the business day preceding the implementation of the rule (Rule 1.41(c)(2)); and
 - ▶ If the DTF provides the Commission with a weekly notice of changes it may place the following rules into effect without prior notice to the Commission (Rule 1.41(e)(1)):
 - ◆ Non-material revisions;
 - ◆ Changes in delivery standard set by third parties;
 - ◆ Changes in index contracts;
 - ◆ Changes in procedures and forms for the purchase sale or transfer of membership or ownership, but not qualifications, rights, or obligations or membership; and
 - ◆ Changes in administrative procedures.
- A DTF may make rule changes regarding daily administration or standards of decorum without notice to or approval from the CFTC.
- An entity seeking recognition as a DTF may request that the CFTC consider under Section 15 of the CEA any of the entity's rules or policies, including operational rules and terms or conditions of products listed for trading, when the DTF is recognized or any period afterwards.

Listing New Products

- A DTF may label a product "Listed for trading pursuant to Commission approval," if the product terms have been approved by the Commission. (Rule 37.4(e)(1)).

- A recognized DTF may list contracts for trading if it files with the Commission a submission which includes the text of the contract's terms or conditions at the same time traders or participants in the market are notified, but in no event later than the close of business on the business day preceding the initial listing. (Rule 5.2).
- A new "cash-settled contract" to be listed for trading by a DTF will be deemed approved within ten business days after reception by the Commission, unless notified within the period, if (Rule 5.3(a)):
 - ▶ The submission is labeled as being submitted pursuant to Commission rule 5.2 – Fast Track Ten-Day Review;
 - ▶ The application is for:
 - ◆ A future contract providing for (i) cash settlement or (ii) for delivery of a foreign currency which there is no legal impediment to delivery and for which there exists a liquid cash market; or
 - ◆ An option contract that is cash settled, is for delivery of a foreign currency which there is no legal impediment to delivery and for which there exists a liquid cash market, or is to be exercised into an already designed contract market or approved futures contract;
 - ▶ The application is not for a commodity listed under section 1a(3) of the CEA or subject to the procedures of section 2(a)(1)(B) of the CEA;
 - ▶ The submitting entity is trading in at least one contract which is not a dormant commodity;
 - ▶ The submission complies with Part 5, App. A. In applications for cash-settled futures contracts, a board of trade shall submit (Part 5, App. A(b)):
 - ◆ Rules setting forth the terms and conditions of the proposed futures contract;
 - ◆ A description of the cash market for the commodity on which the contract is based;
 - ◆ A demonstration that the cash settlement of the contract is at a price reflecting the underlying cash market, will not be subject to manipulation and distortion, and is based on a cash price series that is reliable, acceptable, publically available and timely (this demonstration shall include a completed

copy of the chart listed under Part 5, App. A(b)(3) or the equivalent information in narrative form); and

- ◆ Upon request such additional evidence, information, or data relating to whether the contract complies with the CEA and the Commission's rules and policies, and whether the contract has been or is reasonably expected to be used for hedging and/or price basing;

In applications for option contracts, a board of trade shall submit (Part 5, App. A(c)):

- ◆ Rules setting forth the terms and conditions of the proposed option contract;
 - ◆ For options on futures contracts, the terms and conditions of the proposed or existing underlying futures contract;
 - ◆ For options on physical commodities, a description of the cash market or the commodity on which the contract is based and depending on the method for settling the option, the relevant chart for either a physical delivery or cash settled futures contract;
 - ◆ A completed version of the chart provided under Part 5, App. A(c)(3), which lists information regarding the terms and conditions of the option; and
 - ◆ Upon request any information or data relating to whether the contract complies with the CEA and the Commission's rules and policies;
- ▶ The submitting entity does not make changes in its application except for non-substantial changes or as requested by the Commission; and
 - ▶ The submitting entity has not requested that the application be reviewed under section 6 of the Act.
- A new contract for physical delivery to be listed for trading by a DTF shall be deemed approved by the Commission forty-five days after receipt by the Commission of the application for contract approval, unless notified otherwise within the period, if (Rule 5.3(b)):
- ▶ The submission has been labeled as being submitted pursuant to Commission rule 5.2 – Fast Track Forty-Five Day Review;

- ▶ The application for contract approval is for a commodity other than those subject to the procedures of section 2(a)(1)(B) of the Act;
- ▶ The submitting entity lists for trading at least one contract which is not dormant;
- ▶ The submission complies with Part 5, App. A. In applications for designation of physical delivery future contracts, a board of trade shall submit (Part 5, App. A(a)):
 - ◆ Rules setting forth the terms and conditions of the futures contract;
 - ◆ A description of the cash market for the commodity on which the contract is based;
 - ◆ A demonstration that the terms and conditions will result in deliverable supply such that the contract will not be conducive to price manipulation or distortion and that the deliverable supply reasonably can be expected to be available to short traders and salable by long traders at its market value in normal cash marketing channels (this demonstration shall include a completed copy of the chart listed under Part 5, App. A(a)(3) or the equivalent information in narrative form); and
 - ◆ Upon request such additional evidence, information, or data relating to whether the contract complies with the CEA and the Commission's rules, and whether the contract has been or is reasonably expected to be used for hedging and/or price basing;
- ▶ The submitting entity does not make changes in its application except for non-substantial changes or as requested by the Commission; and
- ▶ The submitting entity has not requested that the application be reviewed under section 6 of the Act.

Special Calls

- ▶ Upon a special call by the Commission, a DTF shall provide the Commission such information related to its business as a DTF, including information relating to data entry and trade details, in the form and manner and within the time specified by the Commission in the special call. (Rule 20.1).
- ▶ Upon a special call by the Commission, each person registered or deemed to be registered as a futures commission merchant that carries or has carried an account for a customer on a

DTF shall provide the Commission with information concerning such accounts or positions carried for the customer as specified by the Commission. (Rule 20.2).

- ▶ Upon a special call by the Commission, any person who enters into or has entered into a contract, agreement, or transaction on a DTF shall provide information to the Commission concerning such contract, agreements, or transactions or related positions on other facilities or markets as specified by the Commission. (Rule 20.3).

Other DTF Regulations

- A DTF shall be deemed the agent of any foreign trader that makes transactions on its facility. The DTF shall inform the foreign trader of this rule before it shall allow the foreign trader to conduct transactions on its facility. This rule shall not apply to a foreign trader who has provided a written copy of an agreement identifying another party domiciled in the United States as its agent. This rule shall not apply to transactions executed through and maintained in accounts carried by a registered futures merchant subject to Rules 15.05 (a), (b), (c), and (d). (Rules 15.05(e), 15.05(f), 15.05(g), and 15.05(h)).
- Each DTF shall keep a record that shows the true name, address, and principal occupation or business of any foreign trader executing transactions on the DTF, as well as any person guaranteeing or exercising control over such transactions. (Rule 1.37(c)). This shall not apply to any transactions executed through and maintained in accounts carried by a registered futures commission merchant or introducing broker required to maintain records of this information under Rule 1.37(a) (Rule 1.37(d)).
- Upon request by the Commission, each DTF shall promptly furnish a current list of the facility's members or owners subject to fitness requirements. (Rule 1.41(f)(i)).

Sections of the CEA and Rules which apply to DTFs

- Despite the general exemption from all of the provisions of the CEA for DTFs in Rule 37.2, DTFs are still subject to the following sections of the CEA (Rule 37.5):
 - ▶ Section 1a, definitions;
 - ▶ Section 2(a)(1), which asserts the jurisdiction of the CFTC, the power to designate a board of trade as a contract market, and stating the liability of a principal for any violation of the Act by itself, or by its agents;

- ▶ Section 4, restricting the trading of futures to contract markets;
- ▶ Sections 4b and 4o, the CEA's anti-fraud provisions;
- ▶ Section 4c, prohibiting transactions that are (i) known as "wash sales," "cross trades," "accommodation trades," or is a fictitious sale or is used to cause any price that is not a true a bona fide price to be reported, registered or recorded, and (ii) option trading outside of the terms and conditions proscribed by the Commission;
- ▶ Section 4g, requiring clearinghouses and contract markets to maintain daily records and make public information as required by the CFTC;
- ▶ Section 4i, requiring any person who trades above a level set by the CFTC, to both report to the CFTC the details of such transactions and to keep books and records of such transactions for review by the CFTC and the Department of Justice;
- ▶ Section 5(6) and 5(7), requiring that before a board of trade is recognized as a contract market: (i) its governing board provides for making effective the final orders of the Commission entered pursuant to section 6(c) and 5a of the CEA. (See directly below for descriptions of 6(c) and 5a), and (ii) the board demonstrates that the transactions for future delivery in the commodity for which approval as a contract market is sought will not be contrary to the public interest;
- ▶ Section 6(c), provides the CFTC with the power to revoke the right of a person to trade on any contract market. Section 6(e) also grants the members of the CFTC powers to investigate violations of the CEA.
- ▶ Section 5a, details the duties of contract markets. Each Contract market shall:
 - ◆ Promptly furnish the Commission copies of all bylaws, rules, regulations, and resolutions made or issued by it or by the governing board thereof of any committee, and of all changes and proposed changes therein (Section 5a(a)(1));
 - ◆ Keep all books, records, minutes, and journals of the contract market and its governing board in a manner that will clearly describe all matters discussed by the contract market, its governing board, committees, subsidiaries and affiliates and reveal any action taken in such matters, and allow inspection at all times by the Commission or the Department of Justice. These records must be kept for at least three years, or longer if proscribed by the Commission (Section 5a(a)(2));

- ◆ Require warehouses where commodities traded on the contract market are delivered or delivered from to keep records of its activity for at least three years, and allow inspections by the Commission or the Department of Justice (Section 5a(a)(3));
- ◆ When ordered by the Commission, the contract market shall provide for a period, after trading in contracts of sale of any commodity for future delivery in a delivery month has ceased, during which contracts of sale of such commodity for future delivery in such month may be satisfied by the delivery of the actual cash commodity. The Commission shall issue such orders when it finds that such periods will prevent or tend to prevent "squeezes" in the market (Section 5a(a)(4));
- ◆ Require that the party making delivery of a commodity on a contract for future delivery give written notice of delivery at least one day before delivery (Section 5a(a)(5));
- ◆ Require all contracts for future delivery of commodities shall provide for delivery of commodities of grades conforming to the United States standards, if the standards have been adopted and promulgated by the Commission (Section 5a(a)(6));
- ◆ Require that receipts issued under the United States Warehouse Act (7 U.S.C.A. §241 et seq.) shall be accepted in satisfaction on any futures contract provided that (i) the receipt be for the kind, quality, and quantity of the commodity specified in the contract, (ii) the warehouse meets the reasonable requirements imposed by the contract market with regards to location, accessibility, and suitability for warehousing and delivery purposes, and (iii) the warehouse is subject to the United States Warehouse Act (Section 5a(a)(7));
- ◆ Enforce all bylaws, rules, regulations, and resolutions made or issued by it or by its governing board or other committee that (i) have been approved by the Commission, (ii) have become effective, or (iii) must be enforced pursuant to any Commission rule, regulation, or order. Contract markets shall revoke and not enforce any of its bylaws, rules, regulations, or resolutions which have been disapproved by the Commission (Section 5a(a)(8));
- ◆ Permit the delivery of any commodity for contracts for future delivery of such grade(s), at such point(s), and at such quality and locational price differentials

as will prevent or diminish price manipulation, market congestion, or any abnormal movement of such commodity in interstate commerce. If the Commission informs a contract market that its rules do not support these goals, the contract market shall have seventy five days to make the changes recommended by the Commission. If the contract market fails to make the recommended changes within seventy-five days, the Commission may change the contract market's rules as necessary to achieve these goals (Section 5a(a)(10));

- ◆ Provide a fair and equitable procedure through arbitration or otherwise (such as by delegation to a registered futures association having rules providing for such procedures) for settlement of customers' claims and grievances against any member or employee of the contract market (Section 5a(a)(11));
- ◆ Submit to the Commission for its prior approval any bylaws, rules, regulations, and resolutions made or issued by the contract market, its governing board, or any of its committees that relate to terms and conditions in contracts of sale to be executed on or subject to the rules of the contract market, except those relating to levels of margin. Each contract market shall submit all other rules to the Commission; however such rules can be made effective ten days after receipt by the Commission. The Commission shall approve all rules it determines not to be in violation of the CEA and the rules issued by the Commission under the CEA. The Commission shall disapprove all rules it determines to be in violation of the CEA and the rules issued by the Commission under the CEA. (Section 5a(a)(12)(A));
- ◆ The Commission shall issue regulations to specify the terms and conditions by which during an emergency, a contract market may make rules effective on a temporary basis by a two-thirds vote of its governing board (Section 5a(a)(12)(B)(i));
- ◆ Provide for disclosure to the contract market and the Commission of any trade, business, financial partnership, cost-sharing agreement, profit-sharing agreement, capital sharing agreement, or other formal arrangement between floor brokers or traders on such contract where the arrangement is material and known to the floor broker or floor trader (Section 5a(a)(13));
- ◆ Provide for meaningful representation of the governing board of the contract market's board of trade of a diversity of interests, and that at least twenty percent of the governing board have experience in commodities or futures trading or have other eminent qualifications to contribute to the board.

Additionally no less than ten percent of the board shall be constituted, where applicable, of farmers, producers, merchants, or exporters of principal commodities traded on the exchange (Section 5a(a)(14));

- ◆ Provide for diversity of membership on all major disciplinary committees to ensure fairness and prevent special treatment. Major disciplinary committee shall include a majority of qualified persons representing a trading status other than that of the subject proceeding, and, where appropriate, qualified persons who are not members of the exchange. Trading status may include the following categories: floor brokers and traders; producers, consumers, processors, and distributors, or merchandisers of commodities; future commission merchants; and members of the aforementioned categories who participate in particular contract markets or principal groups of commodities on a board of exchange (Section 5a(a)(15));
- ◆ Disallow any member who has been found by the Commission, a contract market, a registered futures association, or a court of competent jurisdiction to have committed any violation of the CEA or any other law that would reflect on the fitness of member from serving on any contract market oversight or disciplinary panel for an appropriate period (Section 5a(a)(16));
- ◆ Adopt rules to avoid conflict of interest on the governing board or any disciplinary or oversight committees (Section 5a(a)(17));
- ◆ Maintain and utilize a system to monitor trading to detect and deter violations of the contract market's rules and regulations committed in the making of trades and the execution of customer orders on the floor or subject to the rules of such contract market (Section 5a(b)(1));
- ◆ Accurately record (i) the times of trades in increments of no more than one minute in length and (ii) the sequence of trades for each floor trader and broker (Section 5a(b)(2));
- ◆ Record accurately and promptly the essential data on terms, participants, and times for all trades as required by the Commission by rule, including the time of execution of such trade. Data of these records shall be kept in a form that cannot be altered without the alteration being recorded and continually provides this data to the contract market. The form should identify the time of the trade through a mechanism that records the time automatically when the trade is entered or through another method which capture time in a

manner which will allow the sequence of trades to be determined. (Section 5a(b)(3));

- ▶ Section 5b, providing for the suspension as a contract market of any board of trade which fails to comply with any provisions of the CEA or of the CFTC's rules;
- ▶ Sections 6(a) and 6(b), describing the schedule the Commission will follow in approving and suspending contract markets;
- ▶ Section 6b, granting the CFTC the power to compel contract markets to enforce their rules and punish contract markets, their directors, their officers, their agents or their employees for failing to enforce the contract market's rules;
- ▶ Section 6c, authorizing the CFTC to seek injunctions in federal courts to prevent contract markets from violating the CEA, the CFTC's rules, and to prevent contract markets from restraining trading in futures;
- ▶ Sections 8(a) and 8(c), authorizing the CFTC to publish reports regarding the operations and conduct of contract markets, and the transactions of persons found guilty of violating the CEA or the CFTC's rules;
- ▶ Sections 8a(6), 8a(7), and 8a(8), authorizing the CFTC (i) to communicate with the proper committee of a contract market the full facts of any transactions which the CFTC believes disrupts or tends to disrupt any market or is otherwise harmful or against the best interests of producers, consumers, or investors, or which is necessary or appropriate to effectuate the purposes of the CEA, (ii) to alter or supplement the rules of a contract market insofar as necessary after the contract market fails to modify their rules in response to a request by the CFTC. These rule modifications can include: (A) terms or conditions in contracts of sale to be executed on or subject to the rules of such contract market, (B) the form and manner of executions and sales for future delivery, (C) other trading requirements except rules regarding the levels of margin, (D) safeguards with respect to the financial responsibility of members, (E) the manner, method, and place of soliciting business, including the content of such solicitations, and (F) the form and manner of handling, recording, and accounting for customers' orders, transactions, and accounts, and (iii) to make rules and regulations with respect to persons registered under the CEA but are not members of a contract market as required in the public interest.
- ▶ Section 8c(a), granting the CFTC the power to suspend, expel or discipline any member of an exchange when the exchange fails to act.

- ▶ Section 9(a)(2) and 9(a)(3), declaring it to be a felony for any person: (i) to manipulate or attempt to manipulate the price of any commodity subject to interstate commerce, corner or attempt to corner any such commodity, or to knowingly deliver or cause to be delivered through any means of communication false or misleading or knowingly inaccurate reports concerning conditions that affect or tend to affect the price of a commodity in interstate commerce, or knowingly violate Sections 4, 4b(a) through (e), 4c, or 4o(1) or (ii) or contract market to knowingly make or cause to be made in any filing under the CEA any false or misleading statement with respect to a material fact or to knowingly omit any material fact required to be stated in the filing or necessary to make the statements in the filing not misleading;
 - ▶ Section 9(f), prohibiting insider trading;
 - ▶ Section 14, allowing person to file a complaint about a violation of the CEA or CFTC's rules and be awarded actual damages. Complainants can be awarded punitive damages, if the violation was willful and intentional;
 - ▶ Section 20, which limits the property of a commodity broker in a liquidation under chapter 7 of Title 11;
 - ▶ Section 22, creating a private right of action against any person, except contract markets, licensed boards of trade, or registered futures organizations which violates the CEA, for the actual damages and punitive damages where violations are intentional and willful.
- Furthermore, the following rules issued by the CFTC under the CEA still apply:
 - ▶ Rule 1.3, definitions for terms used in Chapter 1 of Title 17 of the Code of Federal Regulations;
 - ▶ Rule 1.31, setting forth the conditions for keeping books and records under the CEA:
 - ◆ All books and record required to kept under the CEA shall be kept for five years, shall be readily accessible during the first two years, and shall be open to inspection by the Commission or the Department of Justice (Rule 1.31(a)(1));
 - ◆ A copy of any book or record shall be provided to the Commission upon request, at the expense of the party keeping the record. The party shall have the option of furnishing the original records instead of a copy (Rule 1.31(a)(2));

- ◆ If the records are maintained on microfilm, microfiche, or on an electronic storage media, the persons responsible for maintaining these records must (i) have facilities for examination by the Commission or Department of Justice for immediate readable projection or production of stored images, (ii) be ready to provide any reasonable hard copy image that the Commission or Department of Justice may request, (iii) maintain separately "Commission-require records" on the individual medium employed (e.g., sheets of microfilm or a disk), (iv) store a duplicate of the records, at a separate location from the original for as long as the period of time required to maintain the original records, and (v) organize and maintain an accurate index of all information maintained on both the original and duplicate storage media (Rule 1.31(b)(2));
- ◆ All records maintained on an electronic storage media must additionally (i) be able to produce copies of such records upon request by the Department of Justice, (ii) develop and maintain written and operational procedures and controls to oversee the initial entry of required records and any subsequent changes to the original or duplicate record, and (iii) either maintain, keep current, and make available to the Commission and the Department of Justice all information necessary to access records and indexes maintained on the electronic storage media or place into escrow and keep current a physical and logical format of the electronic storage media, the file format of all different information types maintained on the electronic storage media and the source code, documentation, and information necessary to access the records and indexes maintained on the electronic storage media (Rule 1.31(b)(3)); and
- ◆ If any records are stored solely on an electronic storage media, the person required to maintain these records shall contract with a third party technical consultant that will provide the consultant with access to and the ability to download information from the electronic storage media. The Commission shall be able to request from the consultant any records it requires. (Rule 1.31(b)(4)).
- ◆ Rule 1.37, requiring a DTF to maintain information about its customers, (See "Other DTF Regulations" on p. 9);
- ◆ Rule 1.41, regarding rules and amending the rules of DTFs (See "Approval of Rule Changes" on p. 5 and see "Other DTF Regulations" on p.10);
- ◆ Rule 5.3, the process for listing new products (See "Listing New Products" on p. 6);

- ◆ Rule 33.10, an anti-fraud provision for commodities option trading;
- ◆ Part 5, describing the procedures for listing new products by DTFs (See "Listing New Products" on p. 6);
- ◆ Part 20, requiring each DTF to furnish information required by the CFTC upon a special call by the CFTC (See "Special Calls" on p. 9); and
- ◆ Part 37, exempted transactions on DTFs (as detailed throughout this memo).

New Clearing Procedures: Conditions to be Recognized as a Clearing Organization

- All contracts, agreements, or transactions for clearing shall be submitted to a recognized clearinghouse. (Rules 37.2(d), 39.2(a)).
- In order to be recognized by the CFTC as a recognized clearing organization, an entity (Rule 39.3):
 - ▶ Need not be affiliated with a recognized DTF (rule 39.3(a));
 - ▶ Must have rules and procedures relating to its governance and the operation of its clearing function; and
 - ▶ Must initially, and on a continuing basis, meet and adhere to the following fourteen core principles:
 - ◆ Financial Resources: have adequate capital resources to fulfill its guarantee function without interruption in various market conditions;
 - ◆ Participant and Product Eligibility: Appropriate admission and continuing eligibility standards for members or participants in the organization and defined criteria for instruments it will accept for clearing;
 - ◆ Risk Management: Ability to manage the risks associated with carrying out its guarantee function through the use of appropriate tools and procedures;
 - ◆ Settlement Procedures: Ability to complete settlements on a timely basis under various circumstances, to maintain an adequate record of the flow of funds associated with each transaction it clears, and to comply with the terms

and conditions of any permitted netting or offset arrangements with other clearing organizations;

- ◆ Treatment of Client Funds: Adequate standards and procedures designed to protect and ensure the safety of client funds;
- ◆ Default Rules and Procedures: Rules and procedures designed to allow for efficient, fair, and safe management of events when members or participants become insolvent or otherwise default on their obligations to the clearing organization;
- ◆ Rule Enforcement: Adequate arrangements and resources for the effective monitoring and enforcement of compliance with its rules and for resolution of disputes;
- ◆ System Safeguards: An adequate program of oversight and risk analysis to ensure that its automated systems function properly and have adequate capacity, security, and emergency and disaster recovery procedures;
- ◆ Governance: Have fitness standards for owners or operators with greater than ten percent interest or an affiliate of such an owner, and for members of the governing board, and have means to address conflicts of interest in making decisions;
- ◆ Reporting: Provide the Commission with all information necessary for the Commission to conduct its oversight function of the clearing organization's activities;
- ◆ Record Keeping: Maintain full books and records of all activities related to business as a recognized clearing organization in a form and manner acceptable to the Commission for a period of five years;
- ◆ Public Information: Public disclosure of information concerning the rules and operating procedures governing its clearing and settlement systems, including default procedures;
- ◆ Information Sharing: Enter into and abide by the terms of all appropriate and applicable domestic and international information sharing agreements and use relevant information obtained from such agreements in carrying out the clearing organization's risk management program; and

- ◆ Competition: Endeavor to avoid unreasonable restraints of trade or imposing any burden on competition not necessary or appropriate in furtherance of the objectives of the CEA or the regulations thereunder.

New Clearing Procedures: Recognition as a Clearing Organization

- A clearing organization that cleared for at least one nondormant contract on January 1, 2000 will be recognized by the CFTC upon receipt by the CFTC of a copy of the clearing organization's rules and a certification by the clearing organization that it meets the conditions for recognition under this Rule 39.3 (See "New Clearing Procedures: Conditions to be Recognized as a Clearing Organization" on p. 18) (Rule 39.4(a)).
- A clearing organization can also apply for recognition by demonstrating that it meets the conditions for being a Recognized Clearing Organization and by submitting its rules, along with an explanation of how those rules satisfy the requirements for Recognized Clearing Organizations, to the CFTC (Rule 39.4(b)).