

DERIVATIVES

See “CFTC Approves Final Rule Eliminating Certain Reporting and Recordkeeping Requirements for Trade Option End-Users,” “CFTC Extends No Action Relief for SEFs With Respect to Certain Uncleared Swaps Transactions” and “CFTC Issues No Action Relief for EU-Based DCOs Authorized to Operate in EU” in the CFTC section, and “European Commission Adopts Equivalence Decision in Regards to US CFTC-Registered CCPs” and “Draft RTS on Risk-Mitigation Procedures for OTC Derivatives Not Cleared by CCPs Published by EU Supervisory Authorities” in the UK Developments section.

CFTC

CFTC Approves Final Rule Eliminating Certain Reporting and Recordkeeping Requirements for Trade Option End-Users

On March 16, the Commodity Futures Trading Commission unanimously approved a final rule removing reporting and recordkeeping requirements for trade option counterparties that are neither swap dealers nor major swap participants (“Non-SD/MSPs”). The final rule will become effective upon publication in the *Federal Register*.

Once the final rule becomes effective, Non-SD/MSPs will no longer be subject to the following: (1) part 45 reporting requirements in connection with trade options; (2) Form TO annual notice reporting requirements for otherwise unreported trade options (including such unreported trade options for calendar year 2015); and (3) swap-related recordkeeping requirements in connection with trade option activities. Non-SD/MSPs who transact in trade options with SDs or MSPs must still obtain a legal entity identifier and provide such identifier to their SD/MSP counterparties.

As part of the final rule, the CFTC also amends Regulation 32.3(c) to eliminate references to the now-vacated part 151 position limit requirements. The CFTC also will withdraw, upon the effective date of the final rule, CFTC No-Action Letter 13-08, which provided Non-SD/MSPs relief from certain swap-related reporting and recordkeeping requirements in connection with their trade option activities (For a more complete discussion of CFTC No-Action Letter 13-08, see the [Corporate & Financial Weekly Digest](#) edition of April 12, 2013).

The final rule is available [here](#).

CFTC Extends No Action Relief for SEFs With Respect to Certain Uncleared Swaps Transactions

The Commodity Futures Trading Commission’s Division of Market Oversight has extended previously granted relief for Swap Execution Facilities (SEFs) with respect to requirements for certain transactions in uncleared swaps.

CFTC Regulation 37.6(b) requires that a SEF provide each counterparty to a transaction entered into on or pursuant to the rules of the SEF with a written record of all terms of the transaction, which shall legally supersede any previous agreement. Such record will also serve as a confirmation of the transaction. In the adopting release of CFTC Regulation 37.6(b), the CFTC noted that, with respect to uncleared swaps, SEFs can meet this

requirement by incorporating by reference the terms set forth in agreements previously negotiated by counterparties, provided that such agreements were submitted to the SEF ahead of execution.

In response to concerns raised, the CFTC grants relief and will not recommend enforcement action if, in a confirmation provided pursuant to CFTC Regulation 37.6(b), a SEF incorporates by reference terms from previously negotiated agreements between counterparties, without first having been supplied such agreements.

The CFTC also will not recommend enforcement action against a SEF for failure to maintain a copy of agreements incorporated by reference in the SEF's confirmation as otherwise would be required under CFTC Regulations 37.0000, 37.1001, and 45.2(a), or to report certain confirmation data pursuant to Regulation 45.3(a), where such confirmation data is contained solely in underlying agreements that are incorporated by reference.

Such relief is premised upon the SEF-establishing rules, which require:

- a confirmation to state, where applicable, that it incorporates by reference the terms of underlying previously negotiated agreements;
- a confirmation to state that, in the event of inconsistency between the confirmation and an underlying previously negotiated agreement, the terms of the confirmation legally supersede any contradictory terms;
- participants to provide the underlying previously negotiated agreement to the SEF on request;
- the SEF to request from participants the underlying previously negotiated agreements and provide such agreements to the CFTC upon request; and
- the SEF to report primary economic term data pursuant to CFTC Regulation 45.3(a)(1).

Furthermore, in order to take advantage of the CFTC's relief, SEFs may not modify their trading, confirmation, or reporting processes in a manner that would reduce the amount of primary economic terms data reported.

Such relief will be effective until the earlier of (1) March 31, 2017 or (2) the effective date of revised CFTC regulations to establish a permanent and practical SEF confirmation solution.

The CFTC's No Action Letter is available [here](#).

CFTC Issues No Action Relief for EU-Based DCOs Authorized to Operate in EU

Following on a joint statement by the Commodity Futures Trading Commission and European Commission announcing a common approach to the regulation of central counterparties (CCPs), the CFTC published a comparability determination regarding the European Market Infrastructure Regulation (EMIR). The CFTC found that certain EU laws and regulations provide a sufficient basis for an affirmative finding of comparability with respect to certain regulatory obligations applicable to derivatives clearing organization (DCOs) registered with the CFTC and authorized to operate as CCPs in Europe (hereinafter "DCO/CCPs"). On the basis of such comparability determination, the CFTC's Division of Clearing and Risk released a letter detailing no action relief for DCO/CCPs:

- DCO/CCPs will not need to apply CFTC Regulation 39.12(b)(6), which requires that upon a DCO's acceptance of a swap for clearing, the original swap be extinguished and replaced by an equal and opposite swap between the DCO and each clearing member acting as a principal for a house trade or an agent for a customer trade, where neither party is a U.S. clearing member or a futures commission merchant (FCM) clearing member.
- DCO/CCPs will not need to apply the "legally segregated but operationally commingled" account model under Part 22 of the CFTC Regulations to their clearing members that are not FCMs.
- DCO/CCPs will not need to apply CFTC Regulation 39.13(g)(8)(i), which requires that initial margin for customer accounts cleared by an FCM be calculated and collected on a gross basis, to non-FCM clearing member intermediaries.
- DCO/CCPs will not need to collect initial margin at a level greater than 100 percent of its initial margin requirements, as required by CFTC Regulation 39.13(g)(8)(ii), with respect to non-hedge positions of customers of non-FCM clearing member intermediaries.
- DCO/CCPs are not required to apply CFTC Regulation 39.12(a)(2)(iii), which prohibits a DCO from setting a minimum capital requirement of more than \$50 million for any person that seeks to become a clearing member to clear swaps, to non-US clearing members or non-FCM clearing members.

- DCO/CCPs will not need to apply CFTC Regulation 39.12(b)(7), which requires “straight-through-processing” of swaps submitted for clearing, to trades that are not executed on or subject to the rules of a DCM or a SEF and for which neither clearing member is an FCM, a swap dealer, or a major swap participant.
- CFTC Regulation 39.13(h)(5), under which DCOs must require their clearing members maintain written risk management policies and procedures and under which DCMs must obtain information from clearing members regarding their risk, will still apply to DCO/CCPs, although DCO/CCPs may implement different oversight programs for US/FCM clearing members and non-US clearing members.
- DCO/CCPs will be permitted to submit financial statements prepared in accordance with IFRS (as opposed to US GAAP), with periodic reconciliation to assist staff in reviewing the financial statements, in order to satisfy Regulations 39.11(f) and 39.19(c)(3)(ii).

The CFTC’s comparability determination analyzed the requirements of the US and EU regulatory regimes with respect to the financial resources, risk management, settlement procedures and default procedures required of CCPs.

- **Financial resources.** The CFTC found that both regimes regulated the financial resources required of CCPs with the goal of ensuring that CCPs can meet financial obligations to market participants and contribute to the financial integrity of the derivatives markets. The CFTC noted that both regimes include provisions pertaining to resources used to cover a clearing member’s default, the types of acceptable financial resources and regular stress testing.
- **Risk management.** The CFTC found that both regimes had similar risk management provisions that prescribe how CCPs should monitor, evaluate and manage the risks to which they are exposed.
- **Settlement and default procedures.** The CFTC found that both regimes had comparable requirements with respect to CCP settlement procedures (designed to eliminate or strictly limit a CCP’s exposures to settlement risk) and default procedures (requiring timely action to contain losses and liquidity pressures).

The CFTC also seeks to streamline the process by which a EU CCP will register with the CFTC as a DCO. Under the streamline process, a EU CCP may evidence compliance with certain EU regulations in lieu of requiring compliance with CFTC Regulations and may submit documents provided to EU regulators in lieu of certain documents required by the CFTC.

The CFTC’s No Action Letter is available [here](#).

The CFTC’s Comparability Determination is available [here](#).

UK DEVELOPMENTS

EU Commission Adopts Delegated Regulation on Abusive Practices and Suspicious Orders and Transactions Under MAR

On March 9, the European Commission adopted a delegated Regulation (and an accompanying Annex) in relation to the EU Market Abuse Regulation (MAR). The delegated Regulation sets out arrangements, systems and procedures and notification templates to be used for preventing, detecting and reporting abusive practices or suspicious orders or transactions under MAR (STOR requirements). As noted in the [Corporate & Financial Weekly Digest](#) edition of October 2, 2015, the European Securities and Markets Authority (ESMA) published a final report in September 2015 in regards to MAR, which contained several draft regulatory technical standards (RTS), including those related to STOR requirements.

The STOR requirements, contained in the delegated Regulation supplement Article 16 of MAR, require market operators and investment firms operating trading venues to have systems and procedures in place to prevent, detect and report suspicious orders or transactions. It also requires individuals who are professionally arranging or executing transactions to have systems and procedures in place to detect and report suspicious orders or transactions.

Notable requirements in the delegated Regulation include that:

- systems and procedures must “allow for the analysis, individually and comparatively” of “every transaction and order placed, modified, cancelled or rejected” and to produce alerts for further analysis;

- regular and comprehensive training is implemented for staff involved in the monitoring, detection and identification of orders and transactions that could constitute actual or attempted insider dealing and market manipulation, including staff that process orders and transactions; and
- reports of suspicious orders and transactions are made “without delay” once a reasonable suspicion has been formed in relation to a trading behavior, in accordance with the template in the Annex attached to the delegated Regulation (STOR template).

The delegated Regulation will be enacted 20 days following its publication in the *Official Journal of the EU* and is set to go into effect on July 3.

A copy of the delegated Regulation is available [here](#), and the accompanying Annex, containing the STOR template, is available [here](#).

European Commission Adopts Equivalence Decision in Regards to US CFTC-Registered CCPs

See “*CFTC Issues No Action Relief for EU-Based DCOs Authorized to Operate in EU*” in the CFTC section.

On March 15, the European Commission (the Commission) adopted an equivalence decision in regards to US central counterparties (CCPs). The equivalence decision will allow CCPs authorized and registered with the Commodity Futures Trading Commission to apply for recognition under the European Market Infrastructure Regulation (EMIR) to provide clearing services to EU clearing members or trading venues.

The equivalence decision follows a recent announcement by the CFTC and the Commission in February 2016 that they had reached an agreement for a harmonised approach to CCPs.

For further background, see the [Corporate & Financial Weekly Digest](#) edition of February 12, 2016.

A copy of the Commission's equivalence decision is available [here](#).

A copy of the Commission's press release is available [here](#).

Draft RTS on Risk-Mitigation Procedures for OTC Derivatives Not Cleared by CCPs Published by EU Supervisory Authorities

On March 8, the European Supervisory Authorities (which includes the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority and the European Securities and Markets Authority) published final draft regulatory technical standards (RTS) in relation to the European Market Infrastructure Regulation (EMIR).

The draft RTS covers risk-mitigation procedures for over-the-counter (OTC) derivatives contracts not cleared by a central counterparty. The draft RTS requires counterparties to exchange both initial and variation margin on OTC derivatives that are not centrally cleared. The draft RTS also sets out a list of eligible collateral for the margin requirements.

The draft RTS provides for a proportionate implementation of the requirements and is proposed to come into effect on September 1. The requirements will initially apply to the largest counterparties from September 2016, with a four-year phase in for the remaining counterparties.

A copy of the draft final RTS is available [here](#).

The EBA's press release is available [here](#).

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UK DEVELOPMENTS

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