

Corporate & Financial Weekly Digest

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CFTC Announces Multiple Dodd-Frank Rulemakings

Co-authored by [Kenneth M. Rosenzweig](#) and [Christian B. Hennion](#)

The Commodity Futures Trading Commission has issued five rule proposals and an advance notice of proposed rulemaking, five of which relate to rulemakings required by the Dodd-Frank Wall Street Reform and Consumer Protection Act. The sixth is not mandated by the Dodd-Frank Act, and relates to permitted investments of customer funds and funds held in foreign futures accounts.

- **Anti-Manipulation Rule:** Section 753 of the Dodd-Frank Act (which amended section 6(c) of the Commodity Exchange Act (CEA)) expanded the CFTC's anti-manipulation authority. To implement this expanded authority, the CFTC has proposed a new rule, modeled after Securities and Exchange Commission Rule 10b-5, prohibiting certain identified manipulative market practices. The proposed rule would render it illegal, with respect to any market under CFTC jurisdiction, for any person to (1) intentionally or recklessly engage or attempt to engage in a scheme to defraud or any practice which would defraud any person; (2) intentionally or recklessly make or attempt to make an untrue or misleading statement or an omission of material fact; (3) intentionally or recklessly deliver or attempt to deliver (or cause delivery or attempted delivery of) false or misleading crop or marketing information, or a report regarding conditions affecting prices of commodities in interstate commerce; or (4) directly or indirectly manipulate or attempt to manipulate the price of any such instrument.
- **Advance Notice of Proposed Rulemaking and Request for Comment on Disruptive Trading Practices:** Section 747 of the Dodd-Frank Act amended section 4c(a) of the CEA to expressly prohibit certain trading practices disruptive of fair and equitable trading, including engaging in any trading, practice, or conduct on or subject to the rules of a registered entity that (1) violates bids or offers; (2) demonstrates intentional or reckless disregard for the orderly execution of transactions during the closing period; or (3) is, is of the character of, or is commonly known to the trade as, "spoofing" (bidding or offering with the intent to cancel the bid or offer before execution), as well as any other disruptive trading practice prohibited by the CFTC. The CFTC has approved an advanced notice of proposed rulemaking for publication in connection with the implementation of this provision of the Dodd-Frank Act. Among the areas on which the CFTC is requesting public comment are what, if any, additional trading practices should be prohibited as disruptive of fair and equitable trading, whether algorithmic traders should be held

accountable for disrupting markets, and what duties of supervision over trades should be required to prevent disruptive trading practices.

- **CFTC Review of Rule Changes at Exchanges and Clearinghouses:** This proposal would establish a new framework for certification and approval of new products, new rules and rule amendments submitted to the CFTC by registered entities, which now include swap execution facilities and swap data repositories. Under the proposal, a new rule or rule amendment generally will become effective 10 business days after it is received by the CFTC. The CFTC may extend the review period for an additional 90 days if the new rule or rule amendment presents “novel or complex issues,” if it lacks sufficient explanation, or if it is potentially inconsistent with the CEA or the CFTC’s regulations. During that 90-day review period, the CFTC must provide the public with the opportunity to comment on the rule or rule amendment. The proposed rule also would require a “systemically important derivatives clearing organization” to provide the CFTC with a 60-day advance notice of any proposed change to its rules, procedures or operations that could “materially affect the nature or level” of risks presented by that entity, which the CFTC has indicated would include changes to financial resources, participant and product eligibility, risk management, settlement procedures, default procedures, disaster recovery or governance. Finally, the proposed rule would prohibit the listing, trading or clearing of a product that is based on certain excluded commodities and that involves terrorism, assassination, war, gaming, any activity that is unlawful under U.S. state or federal law, or any similar activity that the CFTC determines to be contrary to the public interest.
- **Swap Review Process:** This proposal is intended to implement provisions of the Dodd-Frank Act that require the CFTC to prescribe the processes and criteria for determining the eligibility of derivatives clearing organizations (DCOs) to clear swaps and for determining which swaps will be subject to mandatory clearing. Under the CFTC’s proposal, DCOs would be presumed eligible to clear any swap that is of a category already cleared by that DCO, but would be required to submit a written request to the CFTC for an eligibility determination in order to accept additional categories of swaps for clearing. Such request must address the ability of the DCO to maintain compliance with DCO core principles in connection with the clearing of such swaps, as well as provide certain specific information about such swaps. DCOs would also be required to submit a statement to the CFTC with respect to those swaps that they seek to clear to assist the CFTC in determining whether clearing will be mandatory for such swaps. The statement must address various factors set forth in the Dodd-Frank Act, including outstanding notional exposures and liquidity for the applicable swaps; availability of rules and operational and credit support infrastructures for clearing of such swaps; and the effect of such clearing on the mitigation of systemic risk, among others. The CFTC would have 90 days to review the DCO’s submission and make a determination, including a 30-day public comment period. The proposal also includes a process for the CFTC to initiate reviews of swaps not yet accepted for clearing by a DCO to determine whether clearing should be required.
- **Investment of Customer Funds:** In a rulemaking not mandated by the Dodd-Frank Act, the CFTC has proposed amendments to CFTC Rules 1.25 and 30.7 that would narrow the scope of permissible investments for customer funds held by futures commission merchants. Among other changes, the proposed rule would specify new concentration

limits (instrument-based, issuer-based or both) with respect to all permitted instrument classes other than U.S. treasuries, and would restrict investments in the securities of government sponsored entities and other less-frequently used categories of securities to those instruments that are “fully guaranteed” as to principal and interest by the U.S. government. The proposal would also extend the investment restrictions applicable to customer segregated funds under CFTC Rule 1.25 to customer assets held in connection with positions in foreign futures and options under CFTC Rule 30.7, which currently are not subject to similar investment limitations.

- **Removal of Reliance on Credit Ratings:** Finally, the CFTC has also proposed rule amendments that would eliminate references to credit ratings in several CFTC regulations. Section 939A of the Dodd-Frank Act requires federal agencies to eliminate reliance on credit ratings in federal regulations and replace any references to credit ratings with appropriate standards of credit-worthiness. The CFTC is working with the SEC, the Federal Deposit Insurance Corporation and various other federal regulators to develop uniform standards of credit-worthiness.

The comment periods for the proposals regarding the removal of reliance on credit ratings and the investment of customer funds will expire 30 days from the dates of their respective publications in the *Federal Register*. The comment periods for the remaining proposals described above will expire 60 days from the dates of their respective publications in the *Federal Register*.

Information regarding all of the CFTC proposals, including the text of the *Federal Register* releases, fact sheets and Q&As, can be found [here](#).

Katten Muchin Rosenman LLP
Charlotte Chicago Irving London Los Angeles New York Washington, DC