



SECURITIES INDUSTRY PRACTICE

# ALERT

## COMMODITY FUTURES TRADING COMMISSION PROPOSES NEW CONFLICT OF INTEREST RULES

By Amit Shah

The Commodity Futures Trading Commission recently proposed new rules to implement statutory provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act. The proposed rules relate to the conflicts of interest provisions set forth in section 732 of the Dodd-Frank Act, which amends section 4d of the Commodities and Exchange Act, to direct futures commission merchants and introducing brokers to implement conflict of interest systems and procedures to establish safeguards within the firm. The proposed rules seek to ensure that any person researching or analyzing the price or market for any commodity is separated by appropriate informational partitions. The proposed rules also address other issues, such as enhanced disclosure requirements.

Section 732 of the Dodd-Frank Act requires that futures commissions merchants and introducing brokers “establish structural and institutional safeguards to ensure that the activities of any person within the firm relating to research or analysis of the price or market for any commodity are separated by appropriate informational partitions within the firm from the review, pressure, or oversight of persons whose involvement in trading or clearing activities might potentially bias the judgment or supervision of the persons.” While section 732 could be read to require informational partitions between persons involved in any research or analysis and persons involved in trading or clearing activities, the Commission believes

that the Congressional intent underlying section 732 was primarily intended to prevent undue influence by persons involved in trading or clearing activities over the substance of research reports that may be publicly distributed.

The proposed rule establishes restrictions on the interaction between persons within a futures commission merchant or introducing broker involved in research or analysis of the price or market for any derivative and persons involved in trading or clearing activities. Further, the proposed rules also impose duties and constraints on persons involved in the research or analysis of the price or market for any derivative by, for example, requiring such persons to disclose during public appearances and in any reports any relevant personal interest relating to any derivative the person follows. The proposed rule also prevents futures commissions merchants and introducing brokers from retaliating against a person for producing a report that adversely impacts the current or prospective trading or clearing activities of the firm.

If the proposed rules are implemented, they would require that futures commission merchants and introducing brokers adopt written conflicts of interest policies and procedures, document certain communications between non-research personnel and provide other disclosures. They would also prevent non-

research personnel from reviewing a research report prior to dissemination, except to verify the factual accuracy of the report and provide non-substantive edits. Non-research personnel may only communicate with research personnel through authorized legal or compliance personnel. The firm's business trading unit may not influence the review or approval of a research personnel's compensation and may not influence the research personnel. Futures commissions merchants and introducing brokers must keep a record of each public appearance by a research analyst. The proposed rule

applies to third-party research reports as well, except where the reports are made available upon request or through a web site maintained by the futures commissions merchants or introducing brokers.

While the Commodity Futures Trading Commission is continuing to receive public comments on any aspect of the proposed rule, the Commission is particularly interested in comments about whether the rules should apply to futures commission merchants and introducing brokers of all sizes or whether the nature of the partitions should depend on the size of the firm.

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For more information about the new conflict of interest rules proposed by the Commodity Futures Trading Commission, please contact:

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