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BROKER-DEALER

FINRA Issues Guidance With Respect to Stop Orders and Volatile Market Conditions

On May 26, FINRA issued guidance encouraging firms to review their policies with respect to the use of stop orders during volatile market conditions. The guidance encourages firms to: (1) ensure customers are provided proper disclosures (either through registered representatives or, if a customer is able to enter stop orders online, through prominent disclosures); (2) review the availability or use of stop orders in light of their customer base; and (3) consider whether certain safeguards should be employed.

FINRA proposed that customers be educated with respect to several topics:

- the price at which a stop order is executed is not guaranteed and ultimately may be materially different than the stop price;
- a stop order may be executed during a period of volatility that is short-lived, resulting in a sale at an undesired price where markets stabilize shortly thereafter;
- a sell stop order may exert downward price pressure on a security;
- placing a limit price on a stop order may afford greater certainty as to the price received by the customer; and
- information regarding volatile market conditions.

Firms also should consider whether certain safeguards are appropriate, including education or other alerts to customers prior to order entry, restriction of order entry during certain times of the day, designation of the default stop order type as an order with a limit price, and expiration of good-until-cancelled stop orders.

A copy of FINRA's Regulatory Notice is available here.

DERIVATIVES

See "CFTC Requests Comment on Proposal To Exempt Federal Reserve Banks From Sections 4d and 22 of the CEA," "CFTC Proposes Supplemental Amendments to Position Limits Proposal," "CFTC Issues No-Action Letter for Shanghai Clearing House" and "CFTC Grants Registration to Three Swap Execution Facilities" in the CFTC section.

CFTC

CFTC Requests Comment on Proposal To Exempt Federal Reserve Banks From Sections 4d and 22 of the CEA

On June 2, the Commodity Futures Trading Commission proposed to exempt Federal Reserve Banks that provide customer accounts to systematically important derivatives clearing organizations (SIDCOs) from Sections 4d and 22 of the Commodity Exchange Act (CEA).

As a result, Federal Reserve Banks would be permitted to hold cash, securities and property deposited into a customer account by a SIDCO in accordance with the standards that otherwise apply to Federal Reserve Banks, including permitting SIDCOs to maintain customer accounts with Federal Reverse Banks pursuant to the standard of liability set forth in the Federal Reserve Bank Governing Documents. In addition, the proposal would exempt Federal Reserve Banks from liability with respect to the exempted requirements under the private right of action for damages pursuant to Section 22 of the CEA.

The proposal does, however, require a Federal Reserve Bank to segregate customer funds from proprietary funds of a SIDCO, and to reply to any request from CFTC staff for information regarding the SIDCO account.

Comments may be submitted by fax or email to the Office of Information and Regulatory Affairs until July 5.

The proposed order and request for comment is available here.

CFTC Proposes Supplemental Amendments to Position Limits Proposal

On May 26, the Commodity Futures Trading Commission proposed amendments to its December 2013 speculative position limits proposal regarding 28 core referenced futures contracts.

The proposed rules would allow certain exchanges and swap execution facilities, subject to CFTC review, to recognize and exempt from federal position limits both enumerated and non-enumerated *bona fide* hedges, certain spread positions and certain enumerated anticipatory *bona fide* hedges. The proposal also amends certain definitions, including the definition of (1) *bona fide* hedging position; (2) intermarket spread position; and (3) intramarket spread position. Further, the proposal delays the establishment and monitoring of exchange-set swaps position limits for exchanges that do not have access to sufficient swap position information.

Katten will publish an advisory providing further details on the proposed rules shortly.

The supplemental notice of proposed rulemaking will be open for public comment for 30 days after publication in the *Federal Register*.

The proposed rules are available here.

CFTC Grants Registration to Two Foreign Boards of Trade

On June 1, the Commodity Futures Trading Commission issued Orders of Registration to BM&FFBOVESPA S.A. (BVMF) and Cleartrade Exchange Pte. Limited (Cleartrade), permitting the two Foreign Boards of Trade (FBOTs) to provide their identified members or other participants in the United States with direct access to their electronic order entry and trade matching systems.

BVMF is an FBOT located in São Paulo, Brazil. BVMF will offer direct access for futures and options contracts based upon interest rates, FX, securities and inflation indices, governmental bonds, and physical and energy commodities. BVMF previously offered access under a CFTC no-action letter.

Cleartrade is an FBOT that is wholly owned by the European Energy Exchange (EEX), and registered in Singapore. Cleartrade will offer direct access for futures and options contracts on freight, container, iron ore, steel, coal and fertilizer.

The CFTC press release is available here.

CFTC Issues No-Action Letter for Shanghai Clearing House

On May 31, the Commodity Futures Trading Commission's Division of Clearing and Risk (DCR) issued a no-action letter stating it would not recommend the CFTC take enforcement actions against the Shanghai Clearing House (SHCH) for failure to register as a derivatives clearing organization.

The no-action letter applies to swaps cleared by SHCH and subject to mandatory clearing by the People's Bank of China. However, relief is limited to SHCH's clearing of proprietary trades of US clearing members and their affiliates.

The no-action letter is effective until May 31, 2017.

CFTC Letter No. 16-56 is available here.

CFTC Grants Registration to Three Swap Execution Facilities

On May 26, the Commodity Futures Trading Commission granted full registered status to GTX SEF, LLC (GTX) of Bedminster N.J., TeraExchange, LLC (Tera) of Summit, N.J. and FTSEF LLC (FT) of Great Neck, N.Y. as swap execution facilities (SEFs). Previously, each operated under temporary registration status.

GTX is a Delaware limited liability company specializing in the trading of FX non-deliverable forwards and is an indirect wholly owned subsidiary of Gain Capital Holdings, Inc., a publicly traded company. FT is a New York limited liability company specializing in the trading of FX non-deliverable forwards and is a wholly owned subsidiary of FlexTrade Systems Inc., a private New York corporation. Tera is a Delaware limited liability company specializing in Bitcoin derivatives and is a wholly owned subsidiary of Tera Group, Inc.

Including GTX, Tera and FT, there are currently 21 SEFs fully registered with the CFTC.

The CFTC press release is available here.

NFA Proposes Late Filing Fee for NFA Form PQR and Form PR

The National Futures Association (NFA) has proposed an amendment to NFA Compliance Rule 2-46 that would add a late filing fee of $200 for each business day that NFA Form PQR or Form PR is filed after the applicable deadline. NFA Form PQR and Form PR are required to be filed with the NFA on a quarterly basis by registered Commodity Pool Operators (CPOs) or Commodity Trading Advisors, respectively. For late NFA Form PQRs, the fee will apply at the CPO level and will not be assessed separately for each pool operated by the CPO that has a late filing.

The NFA intends to make the proposed amendment effective ten days after May 31, 2016, unless the Commodity Futures Trading Commission notifies the NFA that it has determined to review the proposals for approval.

The NFA rule submission is available here.

BANKING

Consumer Financial Protection Bureau Releases Proposed Payday Rules

On Thursday, June 2, the Consumer Financial Protection Bureau (CFPB) released proposed rules affecting the payday and short-term loan industry as part of its authority to prohibit the use of unfair or abusive acts and practices in connection with the provision of consumer financial products and services under the Dodd–Frank Wall Street Reform and Consumer Protection Act.

According to the proposal, for short-term loans (loans with a term of 45 days or less), the lender would need to apply a “full payment test” to determine if the applicant has the ability to repay the loan without reborrowing. Under this test, a lender would be required, at the time of the consumer’s application, to determine whether the borrower will be able to pay the full amount of the loan when due. As an alternative, a lender could offer a loan with a “principal payoff option” for loans of up to $500 under certain conditions prescribed by the CFPB to ensure that consumers are not subject to an extended repayment schedule (e.g., the lender would be able to offer two extensions under certain conditions).

Under the proposal, “longer-term loans” are defined as those with terms that exceed 45 days and have an “all in” APR that exceeds 36% that is either secured by a consumer’s vehicle title or gives the lender the right to debit the consumer’s bank account for repayment. For longer-term loans, a lender could apply the “full payment test” described above. A second option permits the lender to use an alternative framework proposed by the CFPB.

Finally, the CFPB has proposed that, for loans covered by the proposed rule, the lender would have to give borrowers advance notice before accessing their account to collect a payment due. After two returns, the lender would be required to obtain a new payment authorization.

Katten will publish an advisory providing deeper analysis of these proposed rules.

Comments are due September 14.

The proposed rules are available here.

UK DEVELOPMENTS

FCA Occasional Paper on "Market-Based Finance" (a.k.a., Shadow Banking)

On May 26, the UK Financial Conduct Authority (FCA) published an occasional paper (Paper) on "market-based finance" (MBF). The Paper, written by staff in the FCA's Chief Economist's Department, expands on the general concept of shadow banking (credit intermediation carried out by non-banks) and focuses on the FCA's concept of MBF—which it notes is set apart from the traditional model of banking because, in MBF, aspects of credit intermediation are carried out and priced on global markets for money and risk.

The FCA's Paper has three objectives, which include:

- to understand the factors that have pushed traditional banking toward a model that is "increasingly global and market-based;"
- to develop a framework to understand how MBF impacts consumer welfare, and to identify any risks; and
- to collate information on recent developments in MBF and discuss any impacts on the FCA as a securities and conduct regulator.

According to the FCA, MBF is "an enormously important part of the financial system" and is "here to stay"—being an important contributor to consumer welfare. The Paper reports that MBF bolsters consumer welfare by (1) giving borrowers access to a range of investors and risk preferences; (2) increasing ease of access to credit; and (3) catering to the needs of a range of investors through customisable products (among others). However, the FCA also concludes in the Paper that MBF is not without significant risks, and can be complex and unstable. The FCA feels that MBF must be properly understood to be regulated, and notes that regulators need access to data in order to determine if policy intervention is necessary.

The Paper is available here.

The FCA's accompanying press release is available here.

EU DEVELOPMENTS

ESMA Publishes Q&A on the Implementation of MAR

On May 30, the European Securities and Markets Authority (ESMA) published a new Questions and Answers document (Q&A) on the implementation of the EU Market Abuse Regulation (MAR.) The Q&A is aimed to assist common supervisory approaches for EU regulators in the practical implementation of MAR.

The Q&A contains only one question so far, which is related to the scope of obligations to detect and report market abuse under Article 16(2) of MAR. The question asks if the obligations of Article 16(2) apply only to Markets in Financial Instrument Directive (MiFID) firms, or if the obligations also include UCITS management companies, alternative investment fund managers (AIFMs) and other firms professionally trading on their own account. ESMA confirms in the Q&A that Article 16(2) of MAR does not just apply to MiFID firms. ESMA notes that "persons professionally arranging or executing transactions" under Article 16(2), includes and applies to buy-side firms (such as AIFMs and UCITS managers), and firms trading on their own account (i.e., proprietary traders).

A copy of the Q&A is available here.

ESMA's accompanying press release is available here.

For additional coverage on financial and regulatory news, visit *Bridging the Week*, authored by Katten's Gary DeWaal.

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