Katten
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BROKER-DEALER

SEC Cautions Securities Laws May Apply to Interests in Virtual Organizations

On July 25, the Securities and Exchange Commission issued a Report of Investigation cautioning that certain offers and sales of digital assets of virtual organizations (e.g., "coin offerings" or "token sales") could be deemed securities offerings and therefore subject to the federal securities laws. More details relating to the Report of Investigation are available in Gary DeWaal's posting in the July 26 edition of *Bridging the Week*. Katten will also publish a separate client advisory on the subject in the near future.

See also "CFTC Grants DCO Registration to LedgerX" in the CFTC section.

DERIVATIVES

See "CFTC Grants DCO Registration to LedgerX," "CFTC Extends Relief From Transaction-Level Requirements for Non-US Swap Dealers," "NFA Adopts Interpretive Notice on Swap Valuation Disputes," and "NFA Adopts 4s Attestation Process for Swap Dealers and Major Swap Participants" in the CFTC section.

ISDA To Publish T+2 Protocol

On September 5, the regular settlement cycle for most securities transactions in the United States will change from three days (T+3) to two days (T+2). In order to assist derivative market participants that have existing equity derivative transactions with payment dates based on T+3, the International Swaps and Derivatives Association (ISDA) has developed the 2017 OTC Equity Derivatives T+2 Settlement Cycle Protocol ("T+2 Protocol"). The T+2 Protocol, which is scheduled for publication on July 28, provides a simple means for parties to amend relevant swap documentation to be consistent with the new T+2 settlement cycle, thus eliminating undesirable mismatches between cash market settlements and payments in equity derivatives after September 5. The T+2 Protocol works like other ISDA protocols, so that an adherent is deemed to have amended its documentation with each other adherent in the manner provided by the protocol.

When published, the T+2 Protocol will be available here.

CFTC

CFTC Grants DCO Registration to LedgerX

The Commodity Futures Trading Commission has issued an order granting LedgerX LLC registration as a derivatives clearing organization (DCO). As specified in the order, LedgerX is permitted to clear fully collateralized digital currency swaps. A transaction will be fully collateralized if LedgerX holds, at all times, funds in the form of the required payment sufficient to cover the maximum possible loss a counterparty could incur upon liquidation or expiration of the contract.

In connection with the order of registration, the CFTC's Division of Clearing and Risk separately issued exemptive relief to LedgerX from complying with certain CFTC regulations based on LedgerX's fully collateralized clearing model and anticipated clearing membership base.

On July 6, LedgerX also was granted an order of registration as a swap execution facility (SEF). LedgerX initially plans to clear bitcoin options listed on its SEF.

LedgerX's order of registration as a DCO is available here. CFTC Letter No. 17-25 is available here.

CFTC Extends Relief From Transaction-Level Requirements for Non-US Swap Dealers

The Division of Swap Dealer and Intermediary Oversight, the Division of Clearing and Risk and the Division of Market Oversight (collectively, the Divisions) of the Commodity Futures Trading Commission have extended relief previously provided in a series of previous no-action letters relating to transaction-level requirements for non-US swap dealers (non-US SDs). Specifically, the Divisions have granted relief to non-US SDs from certain specified "transaction-level requirements" when using personnel or agents located in the United States to arrange, negotiate or execute swaps with non-US persons that are not guaranteed affiliates or conduit affiliates of a US person.

For these purposes, "transaction-level requirements" include the requirements set forth in CFTC Regulations 23.202, 23.205, 23.400 to 23.451, 23.501, 23.502, 23.505, 23.506, 23.610, 23.701 to 23.704, and Parts 37, 38, 43 and 50. To the extent that the counterparty is not a CFTC-registered swap dealer, the "transaction-level requirements" also include the requirements set forth in CFTC Regulations 23.503 and 23.504.

The relief will remain in place until the effective date of any CFTC rule or other formal action addressing whether a particular transaction-level requirement is or is not applicable to any of the transactions described above.

CFTC Letter No. 17-36 is available here.

NFA Adopts Interpretive Notice on Swap Valuation Disputes

National Futures Association (NFA) has adopted an interpretive notice that standardizes the process for filing swap valuation disputes with NFA. As set forth in the interpretive notice, swap dealers (SDs) generally are required to file with NFA notices of unresolved swap valuation disputes involving initial margin, variation margin and/or transaction or portfolio valuations if the amount in dispute exceeds $20 million. The interpretive notice also requires SDs to amend previously filed notices if the amount in dispute has increased or decreased by at least $20 million. SDs also must terminate previously filed notices when the matters are resolved or the amount in dispute falls below $20 million.

NFA's interpretive notice also requires SDs to file the notices through WinJammer and standardizes the information that must be included in the notice, including (as applicable) NFA identifier, legal entity identifier (LEI), dispute reportable date, dispute type, dispute termination date, receiver/payer, disputed amount, CSA/netting agreement identifier, counterparty name, counterparty LEI or privacy law identifier, unique swap identifier, base currency notional amount, base currency code, notional value USD equivalent, asset class, and product type.

The interpretive notice will be effective for dispute notices required to be filed on or after January 2, 2018.

NFA's interpretive notice is available here.

NFA Adopts 4s Attestation Process for Swap Dealers and Major Swap Participants

National Futures Association (NFA) has revised the process by which each swap dealer (SD) and major swap participant (MSP) applicant demonstrates its ability to comply with Commodity Futures Trading Commission regulations implementing Section 4s of the Commodity Exchange Act (4s Regulations), including but not limited to regulations relating to capital and margin requirements, reporting and recordkeeping and business conduct standards. Effective immediately, applicants will demonstrate compliance with each 4s Regulation by submitting an attestation that the applicant has adopted policies and procedures or other appropriate documentation reasonably designed to ensure that the applicant is in compliance with the 4s Regulation.

This 4s attestation process replaces the current, more onerous, process under which each applicant must submit its actual 4s policies and procedures to the NFA for substantive review and feedback. However, if a current applicant already has received an NFA feedback letter on one or more topic areas, the applicant should follow the instructions in the feedback letter.

Finally, prospective applicants also should be aware that, with respect to 4s Regulations relating to risk management, each applicant will be required to submit both an attestation and risk management policies and procedures as required by CFTC Regulation 23.600(b)(4).

More information is available here.

BANKING

Volcker Rule Developments

Although the exact future of the Volcker Rule (Section 13 of the Bank Holding Company Act of 1956) under the Trump Administration is unclear, there have been two recent developments that indicate an effort on the part of regulators to make the Rule easier to live with in the short run.

On July 21, the Board of Governors of the Federal Reserve System (Board), Federal Deposit Insurance Corporation and the Office of the Comptroller of the Currency issued a joint "Statement Regarding Treatment of Certain Foreign Funds under [the Volcker Rule]". The Statement provides foreign banking entities with no-action relief until July 21, 2018 with respect to involvement with "qualifying foreign excluded funds" that might themselves be considered to be banking entities under relevant definitions in the rules implementing the Volcker Rule. This relief is intended to give regulators additional time to craft a permanent solution to concerns that the Volcker Rule requirements and implementing regulations put foreign excluded funds affiliated with foreign banking entities at a disadvantage in competing with foreign excluded funds that are not affiliated with a banking entity. This relief is consistent with the recommendation made in the Treasury Department's June 2017 Report issued pursuant to Executive Order 13772 ("June Report") that "[a]n exemption [from] the Volcker Rule's definition of "banking entity" should be provided for foreign funds owned or controlled by a foreign affiliate of a US bank or a foreign bank with US operations."

The text of the Statement is available here.

On July 24, the Board issued Supervisory Letter 17-5 dealing with "Procedures for a Banking Entity to Request an Extension of the One-Year Seeding Period for a Covered Fund." The Supervisory Letter gives concrete effect to the provisions in the implementing regulations for the Volcker Rule that give the Board the authority to extend, for up to two additional years, the one-year period of time that a banking entity is generally allowed to reduce to 3 percent the level of its investment in a covered fund sponsored by the banking entity. SL 17-5 provides that an application for extension must be made at least 90 days prior to the expiration of the applicable time period, must explain the reasons for the request, and must contain a plan for compliance by the end of the requested extended seeding period. The Board has exclusive jurisdiction over such applications even for banking entities that have a different primary banking regulator.

SL 17-5 is available here.

In a related development, the Financial Stability Oversight Council (FSOC) has announced that the agenda for its Friday, July 28 executive session will include a discussion about the recommendations regarding the Volcker Rule in the June Report.

The announcement from FSOC is available here.

The June Report is available here.

UK DEVELOPMENTS

FCA Publishes Proposals To Extend the Senior Managers and Certification Regime to All UK Financial Services Firms

On July 26, the Financial Conduct Authority (FCA) published a consultation paper (CP) outlining proposals to extend the Senior Managers and Certification Regime (SM&CR) to all firms authorized under the UK Financial Services and Markets Act 2000 (FSMA).

The new regime will essentially replace the FCA's current Approved Persons Regime with a goal of reducing potential harm to consumers and strengthening market integrity. It seeks to encourage a culture of manager-level staff taking personal responsibility and to ensure regulated firms, and all their staff, understand and can determine where responsibility lies.

A baseline of three main requirements will apply to every firm under the FCA's proposed "*core regime*":

1. Senior Managers Regime (SMR): responsibilities of senior managers are to be clearly delineated by a statement of responsibilities and, should something go wrong in their area, they can be personally held to account. Senior managers are to be individually FCA approved and, as at present, will appear on the FCA Register.
2. Certification Regime: at least once per year, firms must certify that individuals not within the SMR are suitable to conduct their role based on their fitness, skill and propriety if their role could significantly impact customers, markets or the firm.
3. Conduct Rules: these will apply to all financial services staff, stipulating that individuals must act with integrity, due care, skill and diligence, be open to and cooperate with regulators, pay due regard to customer interests and treat customers fairly, and observe proper standards of market conduct.

Under the FCA's proposed "*enhanced regime,*" additional requirements will apply for the largest and most complex firms (less than 1 percent of regulated firms).

The CP consultation closes November 3.

The CP is available here.

EU DEVELOPMENTS

ESMA Updates Technical Reporting Instructions on MiFIR Transaction Reporting

On July 20, the European Securities and Markets Authority (ESMA) published an updated version of its technical reporting instructions relating to transaction reporting under the Markets in Financial Instruments Regulation (MiFIR).

MiFIR extends the transaction reporting requirements under the Markets in Financial Instruments Directive (MiFID) in terms of the scope of instruments in which transactions will be required to be reported as of January 3, 2018, as well as the scope of information that should be provided for each transaction. Further details of the transaction reporting regime are set out in the regulatory technical standards (RTS) on reporting obligations under Article 26 of MiFIR.

The Instructions provide information on:

- the overall process for transaction data reporting;
- the common technical format for data submission; and
- the common set of data quality controls to be applied to each transaction report.

The instructions are available here.

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

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UK/EU DEVELOPMENTS

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