



Presents :

Webinar on Proposed CFTC Registration of Foreign
Boards of Trade

January 6th, 2011

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Introduction

- Existing Foreign Boards of Trade (“FBOT”) no-action letters (“NAL”)
 - Background
 - Requirements

- Proposed CFTC rules implementing Dodd-Frank Act*
 - Overview
 - Eligibility
 - Registration requirements
 - Registration procedure for FBOTs with existing no-action letters and for FBOTs for new direct market access
 - Maintaining registration

* Dodd-Frank Wall Street Reform and Consumer Protection Act, Public Law No. 111-203, 124 Stat. 1376 (2010) (“Dodd-Frank Act”).

No-action letters – Background

- Currently, no formal registration process for FBOTS
 - Since 1996, CFTC Division of Market Oversight issued NALs
 - Endorsed by CFTC Policy Statement on October 27, 2006, which formalized the NAL requirements
- Effect of NAL – CFTC will not take enforcement action against an FBOT for failure to register as a designated contract market (“DCM”)
- 38 NALs have been issued to date

No-action letters – Background

- NALs permit direct market access from the U.S. to FBOTs for:
 - (1) Members in the U.S. trading for their own accounts;
 - (2) Members registered as futures commission merchants or who are exempt under CFTC Rule 30.10 and who trade for U.S. customers through the FBOT's trading system; and
 - (3) Commodity pool operators or commodity trading advisors, or which are exempt from such registration, provided that an FCM or Regulation 30.10 firm acts as clearing firm and guarantees without limitation all such trades

No-action letters – Requirements

- In applying for a no-action letter, a FBOT must provide documentation relating to:
 - (1) membership criteria (including financial requirements);
 - (2) various aspects of the automated trading system;
 - (3) the terms and conditions of contracts proposed to be granted access;
 - (4) settlement and clearing (including financial requirements and default procedures);

No-action letters – Requirements

- (5) the regulatory regime governing the foreign board of trade in its home jurisdiction;
 - (6) the foreign board of trade’s status in its home jurisdiction and its rules and enforcement thereof (including market surveillance and trade practice surveillance); and
 - (7) information sharing agreements.
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- Continuing requirement – update CFTC on material changes and trading volume information

CFTC proposed rules – Overview

- The CFTC on Nov. 19, 2010 proposed rules to implement Section 738 of the Dodd-Frank Act, which gives the CFTC authority to require registration by FBOTs with direct market access to U.S.
- New Chapter 48 of CFTC rules would apply to FBOTs which want to permit direct market access from the U.S.
 - Requires FBOT registration
 - Creates FBOT registration process
 - Requires FBOTs with existing NAL to become registered

Rulemaking Deadlines

- Comments on the proposed rules – January 18, 2011
- Implementation of final rules – July 15, 2011
- FBOTs with existing NALs must file within 120 days of effective date of final rule

Proposed eligibility standards

- (1) Has attributes of “established, organized” exchanges
- (2) Adheres to rules prohibiting “abusive trading practices”
- (3) Enforces rules to “maintain market and financial integrity”
- (4) Authorized by regulator which examines “customer and market protections”
- (5) Subject to continued oversight by regulator with authority to “intervene in the market” and share information with the CFTC

Proposed registration requirements

- (1) FBOT and clearing membership standards on financial resources, conflicts of interest, and information barriers regarding material, non-public information

- (2) Automated trading system complies with IOSCO principles
 - Algorithm matches trades fairly, audit trail, demonstrated reliability, disaster recovery, only “approved” contracts available

Proposed registration requirements

- (3) Contracts available in the U.S. are futures, options or *swaps* eligible to be traded on DCM and subject to prior CFTC review
 - Linked contracts (contracts that settle against any price of a U.S. market) have special requirements
- (4) Settlement and clearing complies with Recommendations for Central Counterparties issued by CPSS-IOSCO (which are due to be updated)

Proposed registration requirements

- (5) “Comprehensive and Comparable” supervision and regulation over FBOT and clearing organization by home regulatory authority
 - Regulatory objectives same, on-going oversight of market integrity, customer protection and clearing and settlement

- (6) Sufficient rules, available compliance resources and disciplinary procedures to enforce appropriate trading practices

- (7) Information sharing arrangements among the FBOT, the clearing organization, regulatory authorities

Proposed continuing requirements

- Continuing registration requirements
 - Compliance with eligibility and registration requirements
 - FBOT will require agreement to CFTC jurisdiction by members with direct access and to CFTC access to books and records
 - Appointment by FBOT of agent for service of process
 - If swaps are available, real-time swaps reporting and reporting to a swaps data repository
 - Coordination and information-sharing with CFTC
 - Periodic reporting of trade volumes
 - Notice of material changes to the CFTC
 - Annual certifications

Proposed additional requirements

- Additional conditions for linked contracts
 - Provide daily trading information to the public
 - Adopt comparable speculative position limits
 - Have authority to direct market participants to limit or reduce position
 - Provide CFTC with comparable large trader information, audit trail data on T+1 basis, on-site access, and notice of rule changes, disciplinary notices
 - Agree to take similar emergency action as taken by CFTC

- When expanding access to include additional contracts
 - Ten day prior notice and certification that contract meets requirements

Proposed registration procedure for FBOT with *existing* NAL

- “Limited” registration process for FBOT with current NAL
- Application requires:
 - Identifying registration requirements and appendix items which were previously submitted as part of NAL process and remain current
 - Resubmitting all of the above
 - Submitting any additional information not previously provided
 - Updating previously provided information
- Application must be filed within 120 days from the date of final registration rules

Proposed registration procedure for FBOTS for *new* direct market access

- Electronic application which includes:
 - Materials required by appendix—materials demonstrate compliance with conditions outlined above
 - CEO certification
 - Confidential treatment requests
- CFTC will approve or deny application based on:
 - Eligibility
 - Registration requirements
 - Existence of “comprehensive supervision and regulation” in home country which is comparable to the U.S. system (and previous relevant findings by the CFTC)
- If FBOT is not approved, may re-apply in one year

Issues under consideration by CFTC

- (1) Should CFTC use the same standards for registration as it used for NAL?
- (2) What should constitute “comparable and comprehensive” supervision and regulation by home country authorities?
- (3) How should registration requirements affect FBOTs that currently have no-action relief? Should they be grandfathered or have limited registration?
- (4) How should “direct access” be defined? Should it include other order routing methodologies in addition to direct access to the FBOT’s matching engine, such as sponsored access or automated order routing through an intermediary’s system?

CFTC proposed rules – Conclusion

■ Benefits

- Provides greater legal certainty for FBOTs
- Requirements are similar to current NAL requirements
- Creates a more transparent and standardized process
- Consistent with methods used by foreign regulators

■ Concerns

- “Limited” registration process for FBOTs with existing NALs is extensive
- Registration process for new FBOTs includes additional documentation requirements
- Expands continuing requirements
- Limits CFTC’s discretion and flexibility

Questions?

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FIA Asia

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- Accessing Indian markets: Who gets access, what are the channels, and which are the markets?
- Commodities: Rules and products have been subject to big changes in recent years. What now?

For more information, please visit the FIA Asia website at www.fiaasia.org or contact Vineet Bhatnagar (vineet.bhatnagar@mfglobal.in), or Nick Ronalds (nronalds@fiaasia.org).