



Commodity Markets Council
1300 L St., N.W. Suite 1020
Washington, DC 20005
Tel 202-842-0400
Fax 202-789-7223
www.commoditymktcs.org

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VIA ELECTRONIC SUBMISSION

David A. Stawick, Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C.

**Re: Adaptation of Regulations to Incorporate Swaps
(RIN 3038-AD53)**

Dear Mr. Stawick:

The Commodity Markets Council (“CMC”) appreciates the opportunity to submit the following comments for consideration by the Commodity Futures Trading Commission (“CFTC” or “Commission”) in response to its proposed amendments to Part 1.35(a) of the CFTC’s regulations to require members of designated contract markets (“DCMs”) and swap execution facilities (“SEFs”) to record all oral communications that lead to the execution of transactions in a commodity interest or cash commodity (the “Recording Requirement”).¹

CMC is a trade association that brings together exchanges and their industry counterparts. The activities of our members represent the complete spectrum of commercial end users of all futures markets including energy and agriculture. Specifically, our industry member firms are regular users of the Chicago Board of Trade, Chicago Mercantile Exchange, ICE Futures US, Kansas City Board of Trade, Minneapolis Grain Exchange and the New York Mercantile Exchange. CMC is well-positioned to provide the consensus views of commercial end users of derivatives. Our comments represent the collective view of CMC’s members.

The businesses of all our member firms depend upon the efficient and competitive functioning of the risk management products traded on U.S. futures exchanges. Through the Commission’s diligent oversight efforts that have fostered Exchange innovation and technology adoption, we have seen the commodity markets grow and prosper. They have become deeper and more liquid, narrowing bid/ask spreads and improving hedging effectiveness and price discovery. Meanwhile, liquidity, technology, clearing quality, price and customer service have driven market selection. All of these developments serve the interests of the trade as well as the public.

CMC supports the Commission’s efforts to prevent all forms of market abuse. Nevertheless, we respectfully submit that the Commission has substantially underestimated the considerable costs and limited benefits associated with the Recording Requirement as applied to commercial DCM and SEF members. Accordingly, CMC urges the Commission to withdraw this portion of the Proposed Rule and allow market participants to make and keep only written records for commodity interest transactions and corresponding cash commodity transactions that are hedged with futures or cleared swaps.

¹ 76 Fed. Reg. 33,066, 33,072, Adaptation of Regulations to Incorporate Swaps (Jun 7, 2011) (the “Proposed Rule”).

I. The Proposed Rule

The Proposed Rule would modify Part 1.35(a) to require, among others, *all* members of DCMs and SEFs to record *all* oral and written communications that “lead to the execution of transactions in a commodity interest or cash commodity.”² Moreover, the Proposed Rule would amend Part 1.35(a) to require all members of DCMs and SEFs to save and to index each oral or written transaction record “as a separate electronic file identifiable by transaction and counterparty”³ and to preserve these files for at least five years (and to make these files “readily accessible” for the first two years of that period).⁴

The Commission requested comments on all aspects of the Proposed Rule, including the potential costs and effects of the Recording Requirement.⁵ Many of CMC’s members are non-FCM members of one or more DCMs and expect to be members of SEFs. Although CMC’s members strive to develop and maintain recordkeeping systems that meet all applicable regulatory and industry standards, CMC’s non-FCM members generally do not record oral communication associated with a commodity interest or corresponding cash commodity transaction. Moreover, many of CMC’s members do not currently have in place the technical resources or budget to comply with the Recordkeeping Requirement. CMC has a substantial interest in ensuring that the CFTC’s recordkeeping requirements are effective and commercially practicable. Accordingly, CMC has a substantial interest in the Proposed Rule and respectfully submits these comments to provide the Commission with its perspective on this important issue.

II. The Commission Should Reconsider the Substantial Costs and Limited Benefits of Imposing the Recording Requirement.

The Recording Requirement as proposed is overly broad and will impose new and substantial burdens on many market participants. CMC’s members include commercial businesses that use futures and swaps primarily to hedge commodity price risk. Requiring every commercial member of a DCM or SEF to record its telephone lines (including mobile telephone lines) and to index these recordings according to transaction and counterparty will be tremendously expensive and burdensome - *if not impossible*.⁶

² 76 Fed. Reg. at 33,072. As proposed, Part 1.35(a) would be amended to require:

Each . . . member of a [DCM] or [SEF] [to] keep full, complete, and systematic records, which include all pertinent data and memoranda, of all transactions relating to its business of dealing in commodity interests and cash commodities. . . Included among such records shall be all orders (filled, unfilled, or canceled), trading cards, signature cards, street books, journals, ledgers, canceled checks, copies of confirmations, copies of statements of purchase and sale, and all other records, which have been prepared in the course of its business of dealing in commodity interests and cash commodities, and *all oral and written communications* provided or received concerning quotes, solicitations, bids, offers, instructions, trading, and prices, *that lead to the execution of transactions in a commodity interest or cash commodity*, whether communicated by telephone, voicemail, facsimile, instant messaging, chat rooms, electronic mail, mobile device or other digital or electronic media. 76 Fed. Reg. at 33,090-91.

³ 76 Fed. Reg. at 33,091.

⁴ 76 Fed. Reg. at 33,072.

⁵ 76 Fed. Reg. at 33,076.

⁶ CMC understands that current technology for recording on mobile devices is in its infancy, very limited, and highly unreliable.

Despite this burden, the Proposed Rule contains only a brief and, in many ways, possibly inaccurate analysis of the many costs and perceived benefits associated with the Recording Requirement. CMC is concerned that because the Proposed Rule does not provide any meaningful detail or analysis to justify its cost estimates, the Commission may have inadvertently overlooked many substantial expenses that commercial members of DCMs and SEFs will have to incur if the Recording Requirement adopted in its current form.

For example, the Commission estimates that the cost of the Recording Requirement will be between \$16,750 and \$61,750 initially, plus \$12,600 per year once the recording system is established for every member of a DCM or SEF regardless of whether a particular entity is a small commercial end user that enters into a few trades a month or a large dealer that trades on a continuous basis.⁷ Instead of providing even general reference points to support these seemingly low estimates, the Proposed Rule simply concludes that any costs associated with the Recording Requirement:

would be minimal for the average large . . . DCM or SEF member because the information and data required to be recorded is information and data a prudent . . . DCM or SEF member would already maintain during the ordinary course of its business . . . [and] would be minimal for the average small [introducing broker] or member of a SEF who does not have digital telephone systems in place and may not have robust or up-to-date electronic data saving and storage capacity.⁸

Notably, the Proposed Rule provides no support for its assumption that recording all oral communications that lead to the execution of transactions in a commodity interest or cash commodity is something that prudent large members of DCMs and SEFs currently do in the ordinary course of business. Nor does it provide any justification whatsoever to support its claim that the cost associated with the Recording Requirement would be minimal for smaller entities. On the contrary, CMC believes that the actual cost of complying with the Recording Requirements could be several orders of magnitude higher than the Proposed Rule has projected. However, without notice and an explanation as to how the CFTC performed its cost-benefit analysis, it is impossible for CMC's members or other market participants to fully understand its conclusions.⁹

Indeed, instead of a complete cost-benefit analysis of the Recording Requirement, the Proposed Rule focuses more on economic analyses used to justify *other* regulatory programs adopted in *other* jurisdictions. CMC does not believe that referencing an analogous regulatory program is an appropriate substitute for an individualized cost-benefit analysis of a proposed regulation, particularly where the comparison is based on programs that are not necessarily comparable.

For example, the Proposed Rule includes a detailed description of the Financial Services Authority's ("FSA") recording rule, noting that the FSA's rule requires all "financial service firms" to record any relevant communication by employees on firm-issued or firm-sanctioned telephones, and to

⁷ 76 Fed. Reg. at 33,077.

⁸ 76 Fed. Reg. at 33081. Similarly, the Commission cites to a related rulemaking, stating that "most swap dealers and major swap participants have adequate, existing resources and recordkeeping structures that are capable of adjusting to the new regulatory framework without material diversion of resources away from commercial operations." Reporting, Recordkeeping, and Daily Trading Records Requirements for Swap Dealers and Major Swap Participants, 75 Fed. Reg. 76666, 76673 (Dec. 9, 2010).

⁹ Significantly, the preamble to the Proposed Rule acknowledges that even small entities with limited resources will be subject to the Recording Requirement and, consequently, may be subject to periodic reporting requirements, including responding to subpoenas from the Commission and other federal agencies. It is exceedingly unlikely that any entity would be able to respond diligently to a subpoena requesting all oral and written communications that lead to the execution of transactions in a commodity interest or cash commodity for less than the Commission's estimate of the annual cost of complying with the Recording Requirement (*i.e.*, \$12,600).

keep such records for at least six months in a medium that is readily accessible.¹⁰ According to the Proposed Rule, the FSA reported that an estimated 80% of the telephone lines that would need to be recorded under its rule were already being recorded before the rule became effective.¹¹ Based on this finding, the Proposed Rule suggests that recording telephone lines is such a common practice that requiring the small minority of firms that do not currently record their oral communications to do so could not be considered unreasonable.

CMC believes that such a conclusion is flawed because it is based on incorrect facts and inappropriate assumptions. According to the Proposed Rule, the FSA's recording requirement generally applies only to "financial service firms" conducting customer business. In contrast, the Proposed Rule would apply to *all* members of a DCM or SEF without regard to the entity's size or the nature of its business. Many commodity market participants choose to become members of a DCM primarily because membership provides transaction execution discounts that make hedging less costly. Although they are members of a DCM, these commercial entities are *not* large "financial service firms," they do not conduct customer business, and in most cases, they do not currently record telephone lines.¹² Many more market participants would appear to be subject to the Recording Requirement than are subject to the FSA's recording rule. If the scope of the Recording Requirement and the FSA's recording rule are materially different, any analysis of the cost of these regulations that does not take this difference into account is not accurate.

CMC respectfully submits that adopting the Recording Requirement could impose considerable burdens on many firms that do not currently have in place the technical resources or budget to record, index, and retain every oral communication that leads to the execution of a transaction in a commodity interest or cash commodity. The cost-benefit analysis provided in the Proposed Rule does not take these potential burdens into account. As the Commission understands, an incomplete analysis of the costs associated with a proposed regulation, particularly a proposal as potentially significant as the Recording Requirement, not only increases the risk of adverse unintended consequences, but also does not appear to satisfy minimum procedural requirements under the Administrative Procedure Act.¹³ Accordingly, CMC respectfully requests that the Commission withdraw the Recording Requirement until it reconsiders and provides market participants with adequate notice about the substantial costs associated with this proposed rule.

III. No Recording Requirement is Necessary When a Transaction will be Fully Documented Through Other Means.

The Commission can prevent market abuse effectively using the written records for commodity interest transactions and corresponding cash commodity transactions that members of DCMs are already required to maintain. No new recording requirement for oral communications is necessary when a transaction is fully documented through other means.

In the Proposed Rule, the Commission explains that the Recording Requirement would "harmonize" the CFTC's general recordkeeping requirement in Part 1.35 with the requirements proposed for swap dealers and major swap participants under the Dodd-Frank Act.¹⁴ As proposed, Part 23.202(a)(1) would require "[e]ach swap dealer and major swap participant [to] make and keep pre-

¹⁰ 76 Fed. Reg. at 33072.

¹¹ 76 Fed. Reg. at 33072.

¹² Moreover, because the rules defining what constitutes a SEF and who may qualify as a "member of a SEF" have not been finalized, it is impossible to determine with certainty whether other market participants could be affected by the Recording Requirement.

¹³ See Business Roundtable and Chamber of Commerce of the United States v. SEC, No. 10-1305 (D.C. Cir. 2011).

¹⁴ 76 Fed. Reg. at 33072.

execution trade information, including, at a minimum, records of all oral and written communications provided or received concerning quotes, solicitations, bids, offers, instructions, trading, and prices, that lead to the execution of a swap, whether communicated by telephone, voicemail, facsimile, instant messaging, chat rooms, electronic mail, mobile device or other digital or electronic media.”¹⁵ However, the Commission also explained in the preamble to the proposed reporting and recordkeeping rule for swap dealers and major swap participants that the proposed rule “would *not* establish an affirmative new requirement to create recordings of all telephone conversations if the complete audit trail requirement can be met through other means, such as electronic messaging or trading.”¹⁶ Accordingly, the Commission acknowledges that, although a record of an oral communication may be necessary in some cases, making records of *all* oral communications that lead to the execution of transactions in a commodity interest or cash commodity is not ordinarily required.¹⁷ The Commission should reconcile these two proposals by allowing market participants to make and keep required only written records for commodity interest transactions and corresponding cash commodity transactions that are hedged with futures or cleared swaps.

IV. Conclusion

CMC thanks the Commission for the opportunity to present its views on this most important subject. If you have any questions or would like to discuss further, please do not hesitate to contact me via email at christine.cochran@commoditymkt.com or via telephone at (202) 842-0400 - ext. 101. Thank you in anticipation of your attention to these comments.

Regards,



Christine Cochran
President

¹⁵ Reporting, Recordkeeping, and Daily Trading Records Requirements for Swap Dealers and Major Swap Participants, 75 Fed. Reg. 76,666 (Dec. 9, 2010)

¹⁶ 75 Fed. Reg. at 76,668 (emphasis added).

¹⁷ As the Proposed Rule notes, many futures commission merchants and broker-dealers already record their telephone lines. Because non-clearing members of DCMs and SEFs must execute their exchange-traded orders through a clearing member, any communications associated with these transactions are already available to the Commission through the clearing member. Accordingly, requiring *all* members of DCMs and SEFs to maintain these records independently is, to some extent, duplicative.