FINAL



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VIA ELECTRONIC FILING (http://comments.cftc.gov)

Christopher Kirkpatrick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Re: **Comments of International Energy Credit Association to the CFTC’s proposed “Records of Commodity Interest and Related Cash or Forward Transactions,” 79 Fed.Reg. 68140 (November 14, 2014) RIN 3038—AE23 (the “Proposal”)**

Dear Mr. Kirkpatrick:

The International Energy Credit Association (“IECA”) appreciates the opportunity to submit our comments to the Commodity Futures Trading Commission (“CFTC” or “Commission”) in support of the Commission’s Proposal, which intends to amend CFTC Regulation 1.35(a)[[1]](#footnote-1) to, among other things, formalize the relief under CFTC Letter 14-72 for certain non-registered market participants, including commercial end-users, subject to the rule. For the reasons expressed in Sections B and C of these Comments, the IECA respectfully requests that the Commission expand the relief granted to Customers (Unregistered Members) of designated contract markets (“DCMs”) and swap execution facilities (“SEFs”) by simply removing “member” from the text of Regulation 1.35 and replacing that term with “Commission Registrant.”

If the expanded relief requested in Sections B and C of these Comments is not granted, we also ask in Section D of these Comments that the Commission undertake a more holistic evaluation of how various overlapping recordkeeping rules impact commercial end-users of derivatives, to assure that the rules work together in a rational manner and do not impose unnecessary, inconsistent or duplicative requirements on commercial end-users. In the interim, as a more pressing matter, we have identified three interpretive issues under existing recordkeeping rules (discussed below) that we ask the Commission to please address, so that commercial end-users correctly understand their recordkeeping obligations.

Finally in Section E of these Comments, we offer answers to many of the specific questions which were asked by the Commission or specific Commissioners in the Proposal.

Correspondence with respect to these comments should be directed to the following individuals:

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1. **Background on IECA**

The IECA seeks to protect the rights and advance the interests of the commercial end-user community that makes up the majority of its membership. IECA membership includes representatives of many small and large energy companies all of whom have a fundamental mission of providing safe, reliable, and reasonably priced energy commodities that American businesses and consumers require for our economy and our livelihood. Most of the IECA’s members are representatives of commercial end-users, which rely on swaps to help them mitigate and manage (i.e., hedge) the risks of energy commodity price volatility to their physical energy businesses.

Many IECA members use derivatives to hedge or manage commercial risk, and we anticipate others may wish to do so in the future. For various reasons, a commercial end-user may find that the most cost and price efficient way to trade derivatives offered on a particular DCM or SEF is to become a member of that market. In addition, a particular DCM or SEF may require a person to obtain direct trading privileges, i.e., to become a member, to trade the products that it offers. As a general matter, commercial end-users, including many of the IECA’s members, are not registered or required to register in any capacity with the CFTC, and thus would be considered “Customers” of these markets. In the Proposal, however, the Commission refers to Customers (and potentially others) as “Unregistered Members” (as that term is used in the Proposal) of any DCM or SEF on which they are granted direct trading privileges. The IECA is submitting these comments on behalf of our members as commercial end-users of derivatives or Customers and, therefore, as prospective Unregistered Members of DCMs or SEFs.

1. **Comments**
2. **We Support the Changes to Regulation 1.35(a) set forth in the Commission’s Proposal**

The IECA commends the Commission’s efforts to balance the goals of promoting market integrity and customer protection while eliminating unnecessary burdens on market participants. Consistent with those twin goals, we believe the emphasis under Regulation 1.35(a), in particular for maintaining detailed, searchable audit-trail records, is properly placed on the CFTC registrants that maintain a fiduciary duty while interacting with Customers (i.e., commercial end users) to facilitate their access to DCM and SEF markets as execution and/or clearing intermediaries. Unregistered Members do not have customers – they are the customers. Thus, imposing the full recordkeeping obligations under the rule on them, in our view, would not advance the goal of “customer protection” in any meaningful fashion, but instead would create an unnecessary tax or added cost for Customers using these markets.

For these reasons, we fully support the Commission’s proposal to amend Regulation 1.35(a) to formalize the relief under CFTC Letter 14-72, specifically, to exclude Unregistered Members (i.e., Customers or Non-registrants who become members) of a DCM or SEF from the requirements to maintain records of text messages and to maintain written records required under Regulation 1.35(a) in a manner that is identifiable and searchable by transaction.

We note that in the Proposal (79 Fed.Reg. at 68140), the Commission includes the following statement: “The scope of Regulation 1.35(a) under the Final Rule includes communications made via telephone, voicemail, facsimile, instant messaging, chat rooms, electronic mail, mobile device, or other digital or electronic media. These communications include text messages.” (Emphasis added.)

Based on the foregoing description in the Proposal, the IECA understands that the term “text messages” as used in Regulation 1.35(a)(ii), which indicates that the records required to be kept by Unregistered Members of DCMs or SEFs “do not include text messages sent or received by such member” (emphasis added), is intended to exclude “instant messaging”, “chat rooms,” “mobile devices” and “other digital or electronic media” as the records that contain “text messages” which are not required to be kept by Unregistered Members of DCMs or SEFs under Regulation 1.35(a)(ii).

We also concur with the reasons offered by the Commodity Markets Council leading to CFTC Letter 14-72 and by others at the End-User Roundtable on April 3, 2014, in support of those changes. IECA also generally supports the other changes to Regulation 1.35(a) that the Commission is proposing in its Proposal.

However, for the reasons set forth in Sections B and C of these Comments, the IECA also respectfully requests that the Commission expand the relief granted to members of DCMs and SEFs that are not Commission “registrants,” as more fully described in Sections B and C of these Comments.

1. **Unregistered Members Should Not be Subject to Any of the Requirements of Regulation 1.35(a)**

Without further clarification, the CFTC’s recordkeeping requirements under Regulation 1.35 will unnecessarily overburden Customers using DCMs or SEFs to hedge or mitigate their commercial risks and that should be changed.

Historically, the focus of Regulation 1.35 has been protecting the customer by placing recordkeeping burdens on the fiduciary or broker. Broker was in turn expanded to include “member,” because registered floor brokers or registered floor traders could both transact “customer” executions on the floor – both were still “registrants” of the Commission (or NFA) and both had a fiduciary duty to the customer to execute each customer’s order in a fair and equitable fashion. The term “member” also included FCM, Introducing Brokers, and Commodity Trading Advisors, all of whom held or managed customer monies (again holding fiduciary duty to the customer). At no time in the history of Regulation 1.35 rulemaking has the recordkeeping burden been placed on the “customer” and the amendments made to the Commodity Exchange Act (“CEA”) by the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”) did not give the Commission the authority to expand its jurisdiction under Regulation 1.35 to so impose obligations on the “customer.”

**The IECA submits that if the Commission wants to provide meaningful clarity to Regulation 1.35, then the term “member” should simply be deleted and in its place the term “Commission Registrant” should be inserted, which would then capture those that act in a fiduciary capacity on behalf of their “customers” and would leave “customers” out of the recordkeeping requirements of Regulation 1.35.**

Specifically, CFTC Regulation 1.35 requires in part that “members” of a DCM or SEF shall “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 related cash or forward transactions.” (Emphasis added.) Subject to certain exclusions[[2]](#footnote-2), the general categories of the types of records that will need to be maintained include:

“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 related cash or forward transactions. Among such records each member of a designated contract market or swap execution facility must retain and produce for inspection are all documents on which trade information is originally recorded, whether or not such documents must be prepared pursuant to the rules or regulations of either the Commission, the designated contract market or the swap execution facility. For purposes of this section, such documents are referred to as ‘original source documents.’ Such records shall be kept in a form and manner identifiable and searchable by transaction. Also included among the records required to be kept by this paragraph are all oral and written communications provided or received concerning quotes, solicitations, bids, offers, instructions, trading, and prices that lead to the execution of a transaction in a commodity interest and related cash or forward transactions, whether communicated by telephone, voicemail, facsimile, instant messaging, chat rooms, electronic mail, mobile device, or other digital or electronic media…”

17 C.F.R. 1.35(a). Regarding the uncertainty over the types of records that fit within the above stated category, the IECA shares the concerns filed by the Commercial Energy Working Group (“Working Group”) on October 18, 2013, and strongly supports their request for more clarity from the Commission. As noted by the Working Group, “CFTC Regulation 1.35(a) could subject a member’s entire financial and physical trading business to a heightened recordkeeping standard.” As the Working Group states, this heightened standard is appropriate for entities that handle customer orders being executed on a designated contract market, but should not be expanded so broadly that it captures commercial market participants executing trades on a DCM or SEF exclusively for their own account.

The IECA also directs the Commission to review pages 4 to 16 of the IECA’s submission of April 17, 2014, following the CFTC’s Staff Roundtable to Discuss Dodd-Frank End-User Issues Held on April 3, 2014. The IECA respectfully incorporates its previous comments on Regulation 1.35 by this reference into these Comments.

The IECA believes that the discussion offered by CME Group and the Working Group is directly on point with regards to “execution privileges” versus “trading privileges.” As the Working Group points out, “Trading Privileges is a concept created in the context of contract markets where having trading privileges was the product of having a seat of the trading floor…Those entities that had trading privileges predominately executed futures transactions on behalf of their clients.” The IECA believes that the recordkeeping requirements of CFTC Regulation 1.35 are more meaningful when applied to these types of entities. Accordingly, the IECA supports the CME Group’s and the Working Group’s request that the Commission clarify that a “member” for purposes of Regulation 1.35 excludes entities that are trading on DCMs or SEFs exclusively for their own account.

1. **Comparing the Burdens and Benefits of the Requirements of Regulation 1.35(a) Further Supports Removing Customers (Unregistered Members) from the Requirements of Regulation 1.35(a)**

In addition to the concerns noted above, the IECA is concerned that neither the Proposal nor original Final Rule implementing Regulation 1.35 adequately reviewed the burden Regulation 1.35 would have on Customers. In this regard the Final Rule states[[3]](#footnote-3):

“The amendments will require *members of SEFs* to comply with the regulation 1.35 recordkeeping requirements that are currently followed by FCMs, IBs, RFEDs, and members of DCMs. The Commission anticipates *that members of SEFs will spend approximately eight hours per trading day* (or 2,016 hours per year based on 252 trading days) compiling and maintaining transaction records. According to recent Bureau of Labor Statistics, the mean hourly wage of an employee under occupation code 11-3031, “Financial Managers,” (which includes operations managers) that is employed by the “Securities and Commodity Contracts Intermediation and Brokerage” industry is $80.90. Because members of SEFs may be large entities that may engage employees with wages above the mean, the Commission has conservatively chosen to use a mean hourly wage of $100 per hour. *Thus, each SEF member will have a burden of $201,600 per year (2,016 hours x $100/hour)*. (Emphasis added.)

Although the IECA believes the 8 hours a day is grossly underestimated, even at the cost levels estimated by the Commission ($201,600/year), the burdens of applying Regulation 1.35 to Customers are not justified by the alleged “systemic benefits” of Regulation 1.35, absent the clarifications requested herein by the IECA.

The IECA is concerned with the lack of a comprehensive cost-benefit analysis with respect to imposing the remaining recordkeeping requirements of Regulation 1.35 on Customers (i.e., Unregistered Members). In addition to the cost of recording and surveillance systems sufficient to cover the number of trading personnel involved, and at least one full-time equivalent person dedicated to implementing those systems, there are also consultants’ fees and legal fees required to be incurred with respect to such systems and the records retained thereby. The costs incurred by companies subjected to data requests and discovery in an enforcement investigation by the CFTC or other regulatory agency are perhaps a reasonable approximation of the costs to be incurred in complying with Regulation 1.35 and the costs of responding to such discovery inquiries are invariably a high six-figure amount or larger. Imposing such costs on every Customer (i.e., Unregistered Member) that is a member of a DCM or SEF, when there is no allegation of wrongdoing or enforcement investigation is a significant and onerous expense and, as more fully discussed herein, that expense is not justified by any discernible benefit arising from imposing the recordkeeping requirements of Regulation 1.35 on Customers (i.e., Unregistered Members) trading on a DCM or SEF.

As noted by then-Chairman Gary Gensler in the Appendix to the Final Rule on *Core Principles and other Requirements for Swap Execution Facilities* (the Final Rule that established CFTC Regulation 1.35), “Farmers, Ranchers, producers and commercial companies that want to hedge a risk by locking in a future price or rate would get the benefit of the competition and transparency that trading platforms, both SEFs and designated contract markets (DCMs), will provide.” (Emphasis added.) However, along with these great benefits comes a tsunami of unnecessary record retention requirements that should not apply to farmers, ranchers, producers and commercial companies, i.e., the Customer seeking to use these markets.

Moreover, these unnecessary requirements have already deterred, and will likely continue to deter, participation by Customers on both SEFs and DCMs thereby stifling many of the benefits envisioned by then-Chairman Gensler.

For all the above reasons, the IECA requests that the Commission expand the relief granted to Customers (Unregistered Members) of DCMs and SEFs, by simply removing “member” from the text of Regulation 1.35 and replacing that term with “Commission Registrant.”

1. **Other Comments Regarding Regulation 1.35(a) and Related Issues Under Other CFTC Recordkeeping Rules**

In addition to the concerns expressed in Sections B and C of these Comments, the IECA believes that Regulation 1.35 and other CFTC recordkeeping rules raise a number of other issues for commercial end-users, which are addressed in this Section D of our Comments.

The various recordkeeping rules for commodity interest transactions (including both listed futures/options on futures and swaps) and/or for related cash or forward commodity transactions are interrelated, and the CFTC should approach its review of these rules using a holistic approach to assure that they apply in a rational and consistent manner. For example, the rules vary in delineating the type of information and records a person must capture, in ways that we believe discourage commercial end-users from trading on SEFs,[[4]](#footnote-4) contrary to the Dodd-Frank Act’s objective to migrate trading of swaps to SEFs (or DCMs).

Of pressing concern, we respectfully request the Commission to address the following specific interpretive issues when it finalizes its rulemaking on the Proposal:

* Clarify that the recordkeeping obligations under Regulation 1.35(a), as applied to an Unregistered Member, are limited to (i) such person’s trades in commodity interests on the DCM or SEF on which it is a member and (ii) such person’s cash or physical forward transactions related to such commodity interest trades on the DCM or SEF.
* Clarify that a commercial end-user may voluntarily record conversations without an obligation to maintain such records under Regulation 1.35(a) or under other CFTC recordkeeping rules that may apply to them, i.e., Regulations 18.05, 20.6(c), 32.3(b) or 45.2(b).
* Clarify how the “term of the swap plus five years” record retention requirement under various CFTC rules applies to records relating to an option or swaption that is comprised of multiple underlying options/swaptions that are exercised daily or on another periodic cycle; in particular, to confirm that the five year post-term period applies separately to each constituent option/swaption starting on the date it is terminated, through exercise, expiration or otherwise.
1. **Scope of Commodity Interest Trading and Related Cash or Forward Transactions Covered by Regulation 1.35(a)**

The language of Regulation 1.35(a) creates ambiguity as to the scope of commodity interest trading covered by the rule, which in turn defines the scope of related cash or forward transactions covered by the rule. Specifically, Regulation 1.35(a) requires a member, including an Unregistered 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 related cash or forward transactions.” (Emphasis added.)

Regulation 1.35(a) also provides that a member must, in addition, keep records:

“concerning quotes, solicitations, bids, offers, instructions, trading, and prices that lead tothe ***execution of a transaction in a commodity interest*** and related cash or forward transactions.” (Emphasis added.)

The phrase “business of dealing in commodity interests” as used in Regulation 1.35(a) is undefined and, along with the phrase “execution of a transaction in a commodity interest,” creates uncertainty as to whether an Unregistered Member must keep the records required under the rule with respect to any of its commodity interest trading outside its trading as a member on a particular DCM or SEF.

Specifically, the term “commodity interests” is defined in Section 1.3(yy) to include: “(1) Any contract for the purchase or sale of a commodity for future delivery; (2) Any contract, agreement or transaction subject to a Commission regulation under section 4c or 19 of the Act; (3) Any contract, agreement or transaction subject to Commission jurisdiction under section 2(c)(2) of the Act; and (4) Any swap as defined in the Act, by the Commission, or jointly by the Commission and the Securities and Exchange Commission.” So, we are left to interpret the meaning of the phrase “business of dealing in commodity interests” to understand the extent of a Customer’s (Unregistered Member’s) business that is intended to be capture by this requirement in Regulation 1.35(a).

In reality, we believe the spirit, intention and logic of Regulation 1.35(a) support a narrow reading that Regulation 1.35(a) applies only with respect to an Unregistered Member’s trades in commodity interests on the DCM or SEF on which it is a member and its cash or forward transactions related to those commodity interests traded on such DCM or SEF. The use of the term “business of dealing,” while contributing to the ambiguity, could also be read to imply a nexus to trades occurring on or subject to the rules of a DCM or SEF by a person as a member, thus also supporting the narrow reading.

The uncertainty and risk that the Commission could apply a broader reading discourages commercial end-users from becoming a member of a particular DCM or SEF where access as a member may be the most cost and price efficient means to trade the products offered on that market, or depending on the rules of the DCM or SEF, the only means to trade those products. Regulation 1.35(a) is far more proscriptive in setting out specific audit trail records that a commercial end-user must prepare and maintain compared to other CFTC recordkeeping rules that may also apply to a commercial end-user. A commercial end-user may well refrain from becoming a member of a DCM or SEF when faced with the prospect that doing so could mean it will become subject to the more costly – and we believe unnecessary – recordkeeping burdens imposed under Regulation 1.35(a) with respect to all of its commodity interest trading, including its off-facility (bi-lateral) trading of swaps or trading of commodity interests on other DCMs or SEFs as a non-member.

Thus, we ask the Commission to confirm that Regulation 1.35(a) applies solely with respect to an Unregistered Member’s trades in commodity interests executed on or subject to the rules of the DCM or SEF on which is it a member and such person’s related cash or forward transactions. Alternatively, we ask the Commission to amend Regulation 1.35(a) to explicitly reflect that narrower scope.

On the latter, we propose the following changes to Regulation 1.35(a)(3) for your consideration:

(3) *Provided, however,* for a member of a designated contract market or swap execution facility that is not registered or required to register with the Commission in any capacity~~,~~:

(i) The phrases “business of dealing in commodity interests” and “execution of a transaction in a commodity interest” for purposes of paragraph (a)(1) of this section, refer to the member’s execution of a transaction in a commodity interest on a designated contract market or swap execution facility on which it is a member; and

(ii) Records records required to be kept pursuant to paragraph (a)(1) of this section:

(A) (i) Are not required to be kept pursuant to paragraph (a)(2) of this section; and

(B) (ii) Do not include text messages sent or received by such member.

1. **Treatment of Voluntary Recordings of Oral Conversations Under CFTC Regulation 1.35(a) and Other CFTC Recordkeeping Rules**

A commercial end-user may be subject to recordkeeping obligations under multiple CFTC rules, including Regulations 1.35(a) (if a member of a DCM or SEF), 18.05, 20.6(c), 32.3(b) and 45.2(b), with the overlay of Regulation 1.31 record format, retention and inspection requirements for records maintained pursuant to Regulation 1.35(a) or 18.05 (the “Recordkeeping Rules”). Various Recordkeeping Rules prescribe the types of records that a person is required to maintain, including the information or content to be covered. None of the Recordkeeping Rules imposes an explicit obligation on a commercial end-user to make, or if made, to retain recordings of conversations, putting aside the unlikely scenario of a commercial end-user subject to Regulation 1.35(a) that is registered or required to be registered with the CFTC in some capacity (i.e., that is not an Unregistered Member).

Some commercial end-users find it prudent to record their telephone conversations with their brokers or counterparties for their protection in the event of a dispute with the broker or counterparty, even though they are not required to do so under the Recordkeeping Rules. If a commercial end-user elects voluntarily to record telephone conversations, it is our understanding that those recordings do not become records that such person must now keep under the Recordkeeping Rules, and we believe that is how the rules are widely understood to operate by commercial end-users.

That said, we are aware that some have raised the issue that voluntary recordings may be subject to the Recordkeeping Rules, including the record retention period requirements. We believe such an interpretation, though, is contrary to the Commission’s careful and deliberate decision in its December 2012 amendments to Regulation to 1.35(a)[[5]](#footnote-5) to exclude Unregistered Members from the explicit obligation to record conversations being imposed on various Commission registrants for the first time under that rulemaking. Moreover, it would lead to the illogical result that commercial end-users must retain recordings of conversations for five years, or longer with respect to swap transactions or related cash or forward transactions, whereas CFTC-registrants are required to maintain certain recordings for only one year as provided in Regulation 1.31(a). Faced with that costly recordkeeping burden, a commercial end-user may forgo the sound business practice of recording conversations as a source of evidence that could aid in resolving a dispute with its broker or counterparty. That outcome, too, would be illogical, as contrary to promoting customer protection through use of such a self-help measure.

Such an interpretation is also, in our view, contrary to the Commission’s 1996 *Gilbert v. Lind-Waldock & Co.[[6]](#footnote-6)* decision in which the Commission determined that a person is not required under Regulation 1.35(a) to keep tape recordings it prepares when such records were not ones it was required to prepare. Finally, nothing in the rulemaking history for any of the Recordkeeping Rules suggests the Commission intended to require a person to retain recordings of conversations that the person voluntarily prepares.

In light of the forgoing, we ask the Commission to please confirm our understanding that a commercial end-user may voluntarily record conversations without an obligation to maintain such records under Regulations 1.35(a) (unless it is otherwise expressly required to record conversations as a CFTC-registrant), 18.05, 20.6(c), 45.2(b), 32.3(b) or 1.31.

1. **Clarification of Record Retention Period for Options or Swaptions with Multiple Constituent Parts**

A person that is required under CFTC rules to prepare and maintain records relating to transactions in options, including trading options and swaptions, is generally required to maintain such records through the term of the transaction and for a period of five years thereafter. *See* Regulations 1.31(a), 45.2(c) and 32.3(b).[[7]](#footnote-7) It is unclear to us how the record retention standard applies to records relating to an option or swaption that is comprised of multiple underlying options/swaptions that are exercised daily or on another periodic cycle (a “Serial Option”).

In the energy sector, it is common for a commercial end-user to enter into long term Serial Options with durations of up to 20 years or even longer. If a 20 year Serial Option were treated as one ongoing transaction, the recordkeeping requirement would mandate keeping transaction records for up to 25 years after the individual option or swaption was terminated. Essentially, both ongoing system updates and decommissioned versions and even whole packages would have to be maintained in order to access the year five transaction of a twenty year deal during the time period required by Regulation 1.35.

Therefore, we request clarification that a person may treat each constituent option or swaption in a Serial Option as a separate transaction, with the consequence that the records pertaining to that constituent transaction must be kept for five years following its termination, whether through exercise, expiration or otherwise. We believe that approach strikes an appropriate balance in preserving records useful for market surveillance without imposing unnecessary recordkeeping burdens on commercial end-users.

1. **Answers to Specific Questions Raised in the Proposal Regarding Regulations 1.35**

We offer for your consideration the following answers to many of the specific questions raised in the Proposal.

***1. What are the potential effects of removing the requirement that records of oral and written communications provided or received concerning quotes, solicitations, bids, offers, instructions, trading, and prices that lead to the execution of a transaction in a commodity interest and related cash or forward transactions are not required to be kept in a form and manner that allows for identification of a particular transaction?***

The IECA believes that there would be no material effect on the CFTC’s ability to carry out its market oversight responsibilities by removing the requirement that records be kept in a form that allows for the identification of a particular transaction. In this regard, such records could still be searched by other extraneous information (*e.g.*, date, time, trader, recipients, etc.) similar to how companies would currently conduct searches as part of their ordinary course of business. Moreover, this exclusion would only apply to records “that lead to the execution of a transaction…” (which we believe is too broad of a standard to be effectively applied, particularly by end-users/Unregistered Members). More importantly, however, the records relating to the execution of the transaction would not be impacted by this exclusion.

***2. What are the potential effects of excluding Unregistered Members from the requirement to retain text messages?***

The IECA believes that there would be no material effect on the CFTC’s ability to carry out its market oversight responsibilities by removing the requirement for Unregistered Members to retain text messages. The IECA believes, however, that the exclusion for Unregistered Members should apply to all of 1.35 rather than limiting that exclusion to the provision relating to “text messages.” In this regard, the IECA respectfully suggests that the CFTC either (i) clarify that the definition of “member” in Regulation 1.35 excludes Unregistered Members or (ii) replace the term “member” in Regulation 1.35 with the term “Commission Registrant.”

***3. Is existing technology for storing text messages cost prohibitive for Unregistered Members to use? Are there other impediments to using this technology?***

Yes, the IECA believes that the technology for storing text messages is cost prohibitive. In addition, there are other burden impediments to implementing such software beyond just the software cost. For example, there is training, software implementation, internal auditing/quality checks and ongoing maintenance for any system of storing text messages.

***4. What are the potential effects of excluding Unregistered Members from the requirements to store required records in a form and manner that is searchable and in a form and manner that allows for identification of a particular transaction?***

The IECA believes that there would be no material effect on the CFTC’s ability to carry out its market oversight responsibilities by removing the requirement that records of Unregistered Members be kept in a form that allows for the identification of a particular transaction. In this regard, such records could still be searched by other extraneous information (*e.g.*, date, time, trader, recipients, etc.) similar to how companies would currently conduct searches as part of their ordinary course of business or in response to an enforcement investigation by the CFTC. Moreover, this exclusion would only apply to records “that lead to the execution of a transaction…” Therefore, the records relating to the execution of the transaction would not be impacted by this exclusion.

***5. Rather than excluding all Unregistered Members from these aspects of the written recordkeeping obligations of the rule, would the interests of promoting customer protection and minimizing recordkeeping burdens be better balanced by excluding only small Unregistered Members from these requirements? If so, how would ‘‘small’’ Unregistered Members be defined?***

The IECA believes that since neither small nor large Unregistered Members have “customers” that need to be protected, therefore all Unregistered Members should be excluded. In this regard, the CFTC’s other record retention requirements (*e.g.*, Part 45, etc.) are sufficient to preserve records.

***6. Would the exclusion of text messages from the written records requirement for all Unregistered Members incentivize Unregistered Members, especially commodity trading firms, to switch their method of communication? If so, should the Commission use a certain threshold in setting this exclusion, ensuring that the Commission can continue to properly oversee and monitor the derivatives market and enforce Commission rules and regulations?***

The IECA believes that this exclusion will not create incentives for companies to change their methods of communication. To the extent this occurs in an attempt to evade the Commission’s oversight, the Commission’s anti-evasion authority can be used.

***7. What is the potential effect on the market of excluding members of DCMs or SEFs that are CTAs from the oral recordkeeping requirement of the Final Rule?***

N/A

***8. Is there a significant difference in the administrative burden of the oral recordkeeping requirement of Regulation 1.35(a) for large and small CTAs that would warrant exclusion of small CTAs, but not large CTAs?***

N/A

***9. If so, how would ‘‘large’’ CTAs be defined?***

N/A

***10. Would the Proposal impact the Commission’s ability to carry out its market oversight responsibilities with regard to the overall derivatives market? If so, how?***

The IECA believes that the Proposal would not result in a material effect on the CFTC’s ability to carry out its market oversight responsibilities.

***11. Does the Proposal serve the public interest? In what ways?***

The IECA believes that the Proposal, subject to the recommended changes and comments herein, is in the Public Interest. It allows for a reasonable requirement related to documentation and recognizes that the cost/benefit ratio is out of balance without these changes.  Otherwise, unnecessary compliance costs will be passed on to commercial end-users (i.e., consumers) with little or no measureable benefit.

Questions related to burden:

***“a. What are the costs and benefits to market participants, if any, associated with the Proposal? Please explain and, to the extent possible, quantify these costs.***

The IECA believes that the Proposal will still result in unnecessary 1.35 compliance costs to market participants unless the changes recommended herein are adopted. In order to avoid these unnecessary compliance costs, the CFTC should clarify that Unregistered Members of DCMs or SEFs are excluded from all of Regulation 1.35. In this regard, the CFTC’s record retention requirements that apply to a company should be the same regardless of whether such company transacts for itself on a SEF. The burden is very extensive and large due to the fact that such requirements apply to “all transactions relating to its business of dealing in commodity interests and related cash or forward transactions.” The IECA can find no reason or benefit for subjecting a company to such an extensive and large burden merely because it joined a SEF to conduct its own transactions. Many companies will likely elect to continue entering into transactions for itself on a bilateral basis, rather than elect to enter into transactions for itself on a SEF, in order to avoid the more onerous recordkeeping requirements of Regulation 1.35. Surely, that cannot be the CFTC’s intention with respect to Regulation 1.35, but that is the unintended result!

Accordingly, as proposed in these Comments, the IECA respectfully requests that the Commission either (i) clarify that a “member” for purposes of Regulation 1.35 excludes entities that are trading on SEFs for their own account or (ii) simply replace the term “member” in Regulation 1.35 with the term “Commission Registrant.”

***b. What are the costs and benefits to the public, if any, associated with the Proposal? Please explain and, to the extent possible, quantify these costs.***

The additional compliance costs identified in the response to question “a” above will ultimately be borne by members of the public that purchase the impacted products. In addition, companies that would otherwise use a SEF in order to reduce the price they charges the public may opt to forgo such activity because of the additional regulatory burden the Commission has created. The IECA can find no reason or benefit for subjecting the public to increased costs merely because the seller joined a SEF to conduct its own transactions. Accordingly, the IECA respectfully requests that the Commission amend the definition of “member” as proposed herein.

***c. To what extent does the Proposal protect market participants and the public? How, if at all, could the Proposal be altered to better protect market participants and the public?***

The IECA believes that the Proposal does not go far enough to protect market participants from unnecessary compliance costs. For the reasons discussed above, the IECA respectfully requests that the Commission amend the definition of “member” as proposed herein.

***d. How, if at all, does the Proposal affect the efficiency, competitiveness, and financial integrity of markets?***

The IECA’s members have already seen a reluctance or refusal by market participants to transact their own transactions on a SEF because joining a SEF could expose the company to a tremendous amount of additional compliance costs due to Regulation 1.35. Accordingly, the main impact has been to liquidity on the SEF markets, which directly impacts the efficiency, competiveness and financial integrity” of those and other markets.

***e. How, if at all, does the Proposal affect price discovery?***

The IECA does not believe that the Proposal, nor the changes to the Proposal suggested herein, will have any effect on price discovery. The reporting and record retention requirements that are otherwise applicable to swaps are sufficient for price discovery purposes. Such requirements are sufficient when a company transacts a swap over-the-counter and the requirements should be sufficient for swaps that a company executes for itself on a SEF. The IECA is unaware of any differences in these types of transactions that warrant a change in the record retention requirements.

***f. How, if at all, does the Proposal affect sound risk management for market participants and end-users?***

As discussed in the response to question “d” above, the IECA’s members have already seen a reluctance or refusal by market participants to transact their own transactions on a SEF because joining a SEF could expose the company to a tremendous amount of additional compliance costs due to Regulation 1.35. Therefore, the impact Regulation 1.35 has had on companies is that it has limited their risk management options because many companies are no longer willing to join SEFs.

***g. How, if at all, does the Proposal affect the public interest?***

As discussed in the response to question “b” above, the Proposal will result in increased cost to the public with no offsetting benefit; and, therefore, is not in the public interest.

***h. What are the costs and benefits to market participants and the public, if any, associated with the application of this rule for activities outside of the United States? Please explain, and to the extent possible, quantify these costs.”***

The IECA believes that the misapplication of Regulation 1.35 could result in a reduced number of transactions by non-US persons, which will ultimately impact the liquidity for all market participants, which in turn, will impact members of the public who purchase related goods. In this regard, the IECA agrees with Commissioner Giancarlo’s statement: “The CFTC’s flawed SEF framework is causing a range of unintended adverse consequences. …It is causing non-US persons to stop using the services of US-based support personnel and thereby harming American financial service jobs. …It is also harming relations between the CFTC and foreign regulators. Most seriously, the CFTC’s swaps trading framework is the cause of abrupt fragmentation of global swaps markets between US persons and non-US persons. This has led to smaller, disconnected liquidity pools and less efficient and more volatile pricing and shallower liquidity, posing a significant risk of failure in times of economic stress or crisis.”

Commissioner Giancarlo’s Questions:

**1. The proposal excludes unregistered exchange members from the requirement to retain text messages. Is the scope of this exclusion appropriate? Do the impediments for storing text messages in a searchable format extend to persons beyond unregistered members?**

The IECA believes that the exclusion for Unregistered Members should apply to all of 1.35. The IECA believes that the impediments for storing text messages is generally universal, however, Registered Members may otherwise be better suited to overcome these impediments in a less burdensome manner. In this regard, the IECA defers to the comments filed by such entities.

**2. While unregistered members would not be required under the proposal to keep records in a searchable format, or in a form and manner that allows for identification of a particular transaction, they still would be required to keep all Rule 1.35 records, including all written communications (except text messages) provided or received concerning quotes, solicitations, bids, offers, instructions, trading, and prices *that lead to* the execution of a transaction in a commodity interest and related cash or forward transactions. FCMs, IBs, RFEDs and registered exchange members must keep such records (including text messages) in a searchable format. What are the costs associated with keeping such records in accordance with Rule 1.31? Is *leading to the execution of a transaction* the appropriate scope of this particular recordkeeping requirement? Should the scope be narrowed or broadened? If so, why?**

The IECA believes that converting the Regulation 1.35 records to a searchable format would be costly for its members to implement. As long as the documents are maintained in their original form, the compliance costs under Regulation 1.31(a) are not overly burdensome. However, to the extent a company elects to delete the original and maintain the record pursuant to 1.31(b) and (c), such requirements are greatly outdated, unnecessary and overly burdensome (*e.g.*, there is no reason to require third party consultants, etc.).

Regarding the scope of records “leading to the execution of a transaction,” as discussed herein, the IECA does not believe that such requirement should apply to Unregistered Members.

**3. Are there any technological impediments to the oral recordkeeping requirements of Rule 1.35(a)?**

Yes. If the records have to be searchable, expensive software will need to be obtained and implemented by all impacted parties. The burden is further compounded by the fact that it applies not just to swaps executed on a SEF, but also to certain other transactions.

**4. Is there a need to revise Rule 1.31 given advancements in technology and current business practices?**

As noted in the response to Commissioner Giancarlo’s question 2 above, Regulation 1.31(b) and (c) contain outdated, unnecessary, and overly burdensome requirements for the industry. The Final Rule states that these requirements are intended to ensure that alternative storage is reliable before “original” records can be deleted. Importantly, one of the Final Rules setting up much of the current Regulation 1.31 was issued in 1999, a time when microfilm and microfiche were the norm. *See Final Rule on Recordkeeping*, 64 Fed. Reg. 28735 (May 27, 1999). In this regard, the Final Rule specifically states that Regulation 1.31(b) and (c) are limited to only certain types of storage: “Eligibility for alternative treatment is limited to particular classes of records that are reproduced on microfilm, microfiche…” *See* 64 Fed. Reg. at 28736. Obviously, technology has evolved tremendously since 1999, however, the rule has not. The IECA believes that the protections that were needed to ensure the reliability of alternative storage in 1999 are not the same protections needed today given the light years of advancement in technology. For example, the current rule requires, among other things, that third party consultants be hired (Regulation 1.31(b)(4)) and that companies notify the Commission prior to using alternative storage (Regulation 1.31(c)). As noted in the Commission’s Final Rule from 1999 relating to Regulation 1.31:

“The Commission recognizes the important role improved technology can play in the continued development of the futures industry. Minimizing unnecessary regulatory obstacles to the adopt[ion] of improved technology is a goal of the industry members, customers, and the Commission. Indeed, the pace of technological changes will require the Commission continually to review the standards articulated in this rule to ensure that the recordkeeping requirements reflect to the extent possible the reality of established technological innovation. The Commission therefore welcomes consultation with industry participants and specific proposals regarding how the regulations might be amended in the future to permit the futures industry to use available technology and to respond to the Commission’s legitimate need to have access to complete and accurate records when necessary.“

*See* 64 Fed. Reg. at 28736 (emphasis added). Accordingly, in response to Commissioner Giancarlo’s question, whether Regulation 1.31 needs to be revised “given advancements in technology and current business practices,” the IECA responds: yes and the appropriate response to such advancements in technology should be the subject of a separate rulemaking.

1. **Conclusion**

The IECA supports the Commission’s proposed amendments to Regulation 1.35(a). As more fully explained in Sections B and C of these Comments, the IECA encourages the Commission to expand the relief granted by CFTC Letter 14-72 by simply removing “member” from the text of Regulation 1.35 and replacing that term with “Commission Registrant.”

We also urge the Commission to address the pressing interpretive issues explained in Section D of these Comments as part of its final rule with respect to the Proposal in order to clarify recordkeeping obligations that apply to commercial end-users, including Unregistered Members, under the existing Recordkeeping Rules. It is important for commercial end-users to have a clear understanding of their existing obligations to avoid inadvertent non-compliance.

In addition, we respectfully request the Commission to undertake a more complete, comprehensive reevaluation of the Recordkeeping Rules to assure that the rules work together in a rational manner for futures market participants and swaps market participants, and do not impose unnecessary, duplicative or inconsistent requirements on commercial end-users. We understand that such reevaluation would be a more long term initiative. On behalf of our members, many of which are “small entities” struggling to comply in good faith with the Commission’s rules as they enter into commodity interest transactions to hedge commercial risks of gas and electric utility operations, we look forward to assisting the Commission in such initiative.

The IECA appreciates the opportunity to provide the foregoing comments and information to the CFTC. This letter represents a submission of the IECA, and does not necessarily represent the opinion of any particular member. If you would like for us to expand our discussion of any of the above-listed discussion points, please let us know.

Yours truly,

INTERNATIONAL ENERGY CREDIT ASSOCIATION

/s/ /s/

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1. *Records of Commodity Interest and Related Cash or Forward Transactions*, 79 FR 68140 (Nov. 14, 2014). [↑](#footnote-ref-1)
2. Including, but not limited to, “Oral communications that lead solely to the execution of a related cash or forward transaction.” [↑](#footnote-ref-2)
3. See Adaptation of Regulations to Incorporate Swaps – Records of Transactions, 77 Fed.Reg. 75523 (December 21, 2012) (the “Final Rule”). [↑](#footnote-ref-3)
4. The recordkeeping obligations imposed on an end-user swap counterparty under Regulation 45.2(b) are much more narrowly focused than under Regulation 18.05, which could be triggered by virtue of daily volume of trading of a swap ***on a SEF***, or under Regulation 1.35(a), which could be triggered by virtue of obtaining trading privileges ***on a SEF***. We believe the heightened recordkeeping burdens under Regulations 18.05 and 1.35(a) discourage certain commercial end-users from trading energy swaps on SEFs, and may contribute to the reasons why SEFs have thus far been largely unsuccessful in building trading liquidity in energy swaps. [↑](#footnote-ref-4)
5. *Adaptation of Regulations To Incorporate Swaps—Records of Transactions*, 77 FR 75523 (Dec. 21, 2012). [↑](#footnote-ref-5)
6. [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,720 (June 17, 1996). The Commission rejected a Judgment Officer’s determination that Lind-Waldock, a registered futures commission merchant, violated Regulation 1.35(a) by not retaining tape recordings it prepared of conversations with a futures customer. See footnote 23 of the decision. [↑](#footnote-ref-6)
7. This standard does not, however, apply to a person subject to recordkeeping obligations with respect to certain physical commodity swaps or swaptions under CFTC Regulation 20.6(c). Instead, it is permitted to keep the records in accordance with its recordkeeping schedule and in its normal record retention format, in lieu of following the requirements of Regulation 1.31. Such a person, though, would also likely be subject to recordkeeping obligations relating to its physical commodity swaps and swaptions under Regulation 45.2, which in contrast imposes the “term plus five years” record retention period. This is an example of inconsistent, duplicative requirements that commercial end-users face under the Recordkeeping Rules. [↑](#footnote-ref-7)