



U.S. COMMODITY FUTURES TRADING COMMISSION

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Office of General Counsel

June 7, 2012

Cass R. Sunstein
Administrator
Office of Information and Regulatory Affairs
Office of Management and Budget
Executive Office of the President
725 17th Street, NW
Washington, DC 20503

Re: Second Status Report on "Phase One" of the Commodity Futures Trading Commission's Plan for Retrospective Review of Agency Regulations under Executive Order 13563

Dear Administrator Sunstein:

This is further to apprise you of the status of "Phase One" of the Commodity Futures Trading Commission's ("CFTC" or "Commission") Plan for Retrospective Review of Agency Regulations under Executive Order 13563 ("CFTC Plan" or "Plan").¹ The CFTC, an independent regulatory agency, voluntarily developed the Plan and published it in the Federal Register on June 30, 2011 (76 FR 38328, June 30, 2011) (entitled "Reducing Regulatory Burden: Retrospective Review under E.O. 13563"). In addition, as part of its ongoing efforts to implement the Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act"), the CFTC has had the opportunity to modernize a significant portion of its regulatory scheme.

The CFTC Plan

The CFTC's Plan consists of two phases. In its Federal Register release, the CFTC observed that "[i]n determining the extent to which [the CFTC's] existing regulations have needed to be modified to conform to the Dodd-Frank Act's new requirements, the Commission already has subjected many of its rules to scrutiny." Accordingly, the CFTC stated, "Phase One" of the Commission's retrospective review of its existing

¹ On November 7, 2011, the CFTC submitted to your Office its first status report on Phase One of the CFTC Plan.

regulations is (and has been) well underway as a significant effort prior to the issuance of Executive Order 13563 and the [February 2, 2011] OIRA Memorandum.”

CFTC Status Report Update (since November 2011 Status Report)

Since the initial issuance of its Plan, the CFTC has examined and revised a number of its existing regulations as part of its implementation of the Dodd-Frank Act.

Such final rules, issued since the CFTC’s first status report to OIRA in November 2011, include:

--Final Rules Regarding Core Principles and other Requirements for Designated Contract Markets, 17 CFR Parts 1, 16, and 38

Although not yet published in the Federal Register, the CFTC has adopted new and revised rules, guidance, and acceptable practices governing the designation and operation of designated contract markets (DCMs). The rules, guidance, and acceptable practices implement the core principles for DCMs that were amended by the Dodd-Frank Act and incorporate the trading and execution of swaps on DCMs. To implement the relevant provisions of the Dodd-Frank Act, this rulemaking codifies new and amended rules applicable to DCMs and DCM applicants under the Commission’s Part 38 Rules.

The Commission adopted a number of new provisions to codify standard or commonly-accepted industry practices. In this rulemaking the Commission also provided guidance and acceptable practices for DCMs. “Guidance” provides market participants with information as to how the core principles may apply in various circumstances. “Acceptable practices” provide examples of how the core principles can be satisfied without establishing a mandatory means of compliance.

--Final Rule re Commodity Options, 17 CFR Parts 3, 32, 33 (77 FR 25320 (April 27, 2012))

Because the Dodd-Frank Act definition of a swap includes commodity options, the Commission substantially amended its regulations regarding commodity options, generally subjecting all commodity options that are swaps to the same rules that are applicable to other types of swaps. The Commission provided an exception for trade options to permit parties to hedge or otherwise enter into these types of transactions for commercial purposes. Pursuant to the trade option exemption, which was issued as an interim final rule, if the offeror, the offeree, and the characteristics of the option transaction meet the requirements of the trade option exemption specified in the rule, such option transaction will be exempt from the general Dodd-Frank swaps regime, subject to specified ongoing conditions and compliance requirements.

In its review of existing regulations, the Commission determined that certain of its swaps regulations were no longer necessary. For example, because the Commission determined that the "dealer option" business has, as a practical matter, not existed since the early 1990s, it concluded that there was no longer a need for a rule "grandfathering" activity in such options from a ban on such transactions. The Commission also determined that the ban itself had outlived its usefulness and it, too, was eliminated from the Commission's regulations. Similarly, the Commission removed from its existing regulations a ban on unlawful representations in connection with order execution because, among other things, the transactions to which it originally applied have themselves been banned for more than three decades.

--Final Rule re Commodity Pool Operators and Commodity Trading Advisors: Compliance Obligations, 17 CFR Parts 4, 145, and 147, 77 FR 11252 (February 24, 2012); correction 77 FR 17328 (March 26, 2012))

In this rulemaking the Commission amended its Part 4 regulations, including the promulgation of a new regulation regarding commodity pool operators (CPOs) and commodity trading advisors (CTAs). The Commission reconsidered the level of regulation for CPOs and CTAs participating in the commodity futures and derivatives markets in light of the recent financial crisis and the regulatory reforms under the Dodd-Frank Act.

To oversee more effectively its market participants and the risks such participants may pose to the markets, the Commission decided to revise the requirements for determining which persons or entities should be required to register as CPOs. To that end, the Commission rescinded or modified several exemptions and exclusions from the Commission's registration requirements. Moreover, in the amendments to the Part 4 regulations, the CFTC adopted new data collection requirements for CPOs and CTAs that are consistent with a data collection required under the Dodd-Frank Act for entities registered with both the CFTC and the Securities and Exchange Commission (SEC). The data collection will improve accountability and increase transparency regarding the activities of CPOs and CTAs and facilitate the Commission's efforts to assist the Financial Stability Oversight Council, of which the CFTC, along with several other federal financial regulatory agencies, is a member.

Additionally, the amendments include new risk disclosure requirements for CPOs and CTAs regarding swap transactions.

--Final Rule re Investment of Customer Funds and Funds Held in an Account for Foreign Futures and Foreign Options Transactions, 17 CFR Parts 1 and 30 (76 FR 78776 (December 19, 2011))

Regulation 1.25, which dates back to the late 1930s, identifies the permitted types of investments for customer funds held by Futures Commission Merchants (FCMs) and Derivative Clearing Organizations (DCOs) under CEA Section 4d.

Over the previous several years, the Commission had expanded the types of permissible investments for customer funds under Rule 1.25. In this rulemaking, the Commission reviewed and reconsidered the types of permissible investments and standards for the investment of customer funds, particularly with respect to investments in money market mutual funds, investments in foreign sovereign debt, and the use of in-house repurchase agreements. Under its updated standards, the Commission has (1) narrowed the scope of investment choices, (2) raised certain standards imposed on permitted investments individually and on a portfolio basis, and (3) increased safety by promoting diversification.

In this rulemaking, the Commission noted that recent events in the economy have underscored the importance of conducting periodic reassessments and, as necessary, revising regulatory policies to strengthen safeguards designed to minimize risk, while retaining an appropriate degree of flexibility and opportunities for capital efficiency for DCOs and FCMs investing customer segregated funds.

--Final Rule re Position Limits for Futures and Swaps, 17 CFR Parts 1, 150, and 151 (76 FR 71626 (November 18, 2011))

In this rulemaking the Commission established a position limits regime for twenty eight exempt and agricultural commodity futures and option contracts and the swaps that are economically equivalent to such contracts. In addition to adopting new regulations to implement the congressional mandate to establish position limits, the Commission reviewed and updated related existing regulations. Specifically, the Commission reviewed and updated Commission regulations: (i) setting position limits (Commission regulation 150.2); (ii) defining and implementing the exemption for bona fide hedging (Commission regulations 1.3(z), 1.47, and 1.48); and (iii) imposing aggregation standards (Commission regulations 150.1 and 150.4). In doing so, the Commission reviewed past practices and existing requirements and discarded unnecessary or outmoded regulations in favor of regulations more consistent with current practices and the congressional mandate.

--Final Rule re Derivatives Clearing Organization General Provisions and Core Principles, 17 CFR Parts 1, 21, 39, and 140 (76 FR 69334 (November 8, 2011))

This rulemaking implemented certain provisions of Titles VII and VIII of the Dodd-Frank Act governing derivatives clearing organization (DCO) activities. These regulations establish regulatory standards for compliance with fifteen DCO Core Principles: A (Compliance), B (Financial Resources), C (Participant and Product Eligibility), D (Risk Management), E (Settlement Procedures), F (Treatment of Funds), G (Default Rules and Procedures), H (Rule Enforcement), K (Recordkeeping), L (Public Information), M (Information Sharing), N (Antitrust Considerations), and R (Legal Risk), as set forth in Section 5b of the Commodity Exchange Act (CEA).

The CFTC also updated and added related definitions; adopted rules for DCO chief compliance officers (CCOs); revised procedures for DCO applications, including the

required use of a new Form DCO; adopted procedural rules applicable to the transfer of a DCO registration; and added requirements for approval of DCO rules establishing a portfolio margining program for customer accounts carried by a futures commission merchant (FCM) that is also registered as a securities broker-dealer (FCM/BD). Additionally, the CFTC adopted certain technical amendments to Parts 21 and 39 and certain delegation provisions under Part 140.

The new rules systematize CFTC and industry past practices and expectations. For example, the Commission created and adopted a Form DCO to standardize and clarify the information sought by the CFTC from DCO applicants. In doing so, the Commission relied, among other things, upon nearly ten years of DCO registration experience to create a form designed to streamline the registration process. The Commission further improved its DCO regulations in that the new rule codifies the minimum period for DCOs to liquidate a defaulting clearing member's positions. In crafting these rules the Commission considered current industry practices and adopted rules that prescribe a one-day liquidation period for swaps based on physical commodities and a five-day liquidation period for other swaps.

Going Forward

In the near future, the Commission will continue to consider proposed and final rules to implement the Dodd-Frank Act. During this period, Phase One of the Commission's retrospective review plan will continue, and the Commission will review existing regulations as part of its implementation of the Dodd-Frank Act. The CFTC will continue to review the comments it receives with respect to specific Dodd-Frank Act implementing proposals as well as the conforming amendments that it has proposed.

As the CFTC stated in the Federal Register release publishing its Plan, "[a]fter the substantial completion of the promulgation of final rules under the Dodd-Frank rulemaking process, including the revision of various existing Commission regulations to conform to the requirements of the Dodd-Frank legislation, the Commission intends to begin the process of the periodic, retrospective review of the remainder of its regulations (*i.e.*, those regulations that were not reviewed as part of the Dodd-Frank effort)." This latter process will constitute "Phase Two" of the Commission's retrospective review.

Sincerely,



Dan M. Berkovitz

General Counsel

Commodity Futures Trading Commission