

Client Update

CFTC Eliminates Reporting and Recordkeeping Requirements for End-Users of Trade Options

NEW YORK

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On March 16, 2016, the Commodity Futures Trading Commission (the “CFTC”) adopted final rules (the “Final Rules”)¹ that eliminate the reporting and recordkeeping requirements applicable to entities that are not swap dealers or major swap participants (“non-SD/MSPs”) and that enter into trade options.

Consistent with the CFTC’s proposed rules issued in May 2015 (the “Proposed Rules”),² the Final Rules eliminate (1) the Form TO annual notice reporting requirement for otherwise unreported trade options entered into by non-SD/MSPs; and (2) the reporting requirements in part 45 of the CFTC regulations for all trade options entered into by non-SD/MSPs.

With respect to recordkeeping, the Final Rules eliminate the requirement that a non-SD/MSP must comply with the part 45 recordkeeping requirements in connection with trade options, provided that such a non-SD/MSP counterparty must obtain a legal entity identifier (“LEI”) and provide such LEI to each of its counterparties that is a swap dealer (“SD”) or major swap participant (“MSP”).

The Final Rules became effective on March 21, 2016.

BACKGROUND

The term “swap” under the Commodity Exchange Act (“CEA”) includes commodity options. In April 2012, the CFTC adopted final part 32 rules on

¹ The text of the Final Rules is available at:
<https://www.federalregister.gov/articles/2016/03/21/2016-06260/trade-options>.

² For additional information on the Proposed Rules, please see our client update, “CFTC Proposes to Reduce Reporting and Recordkeeping Requirements for End-Users of Trade Options,” <http://www.debevoise.com/insights/publications/2015/05/cftc-proposes-to-reduce-reporting>.

commodity options, which require, in general, that commodity option transactions be conducted in compliance with the same rules applicable to any other swap.

At the same time, the CFTC adopted an interim final rule providing an exception to this general rule for physically settled commodity options on exempt commodities (such as energy and metal commodities) and agricultural commodities (such as grain and soft commodities) entered into by commercial users of such physical commodities, subject to certain conditions (the “trade option exemption”).³

While most swap regulations do not apply with respect to trade options that satisfy the conditions for the exemption, CFTC regulation 32.3(c) provides that part 20 (large trader reporting) and all applicable antifraud and anti-manipulation provisions will apply to all trade option counterparties and that subparts F and J of part 23 (certain recordkeeping, reporting and risk management duties), part 45 (certain recordkeeping and reporting requirements) and section 4s(e) of the CEA (capital and margin requirements) will apply to all SDs and MSPs with respect to their trade options.

FINAL RULES

Prior to the adoption of the Final Rules, non-SD/MSPs, like SDs and MSPs, were required to comply with the part 45 recordkeeping requirements and, in certain circumstances, with the part 45 reporting requirements with respect to their trade options. In response to comments from market participants asserting that certain part 32 requirements are overly burdensome for commercial end-users, the Final Rules eliminate these and other recordkeeping and reporting requirements for non-SD/MSP trade option counterparties.

³ In order to rely on the trade option exemption, (1) the offeror of a commodity option must be either an eligible contract participant or a producer, processor or commercial user of or merchant handling the commodity that is the subject of the commodity option or the products or by-products thereof, and such offeror must be offering or entering into the commodity option solely for purposes related to its business as such; (2) the offeree must be (and the offeror must reasonably believe the offeree to be) such a producer, processor, commercial user or merchant of such commodity, and must be offered or entering into the commodity option solely for purposes related to its business as such; and (3) the commodity option must be intended to be physically settled.

For additional information on the CFTC’s final rule on commodity options and the interim final rule on the trade option exemption, please see our client update “CFTC Final Rules on Commodity Options,” available at:

<http://www.debevoise.com/insights/publications/2012/04/cftc-final-rules-on-commodity-options>.

Reporting

The Final Rules amend CFTC regulation 32.3(b) such that a non-SD/MSP will not be subject to part 45 reporting requirements with respect to its trade option activities, and will not be required to report otherwise unreported trade options on Form TO. (The Final Rules also delete Form TO from appendix A to part 32.)

The Final Rules do not impose the notice condition in the Proposed Rules that would have required a non-SD/MSP counterparty to provide notice to the CFTC's Division of Market Oversight for trade options with an aggregate notional value in excess of \$1 billion in any calendar year.

Recordkeeping

The Final Rules amend CFTC regulation 32.3(b) such that a non-SD/MSP will not be subject to part 45 recordkeeping requirements with respect to its trade option activities, provided that a non-SD/MSP counterparty must obtain an LEI (under CFTC regulation 45.6) and provide such LEI to each of its counterparties that is an SD or MSP. Therefore, non-SD/MSP counterparties are not required to identify their trade options on their books using a unique swap identifier or a unique product identifier.

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Please do not hesitate to contact us with any questions.