

This Week in Derivatives

December 20, 2024

From the Derivatives Practice Group: The CFTC approved a final rule regarding safeguarding and investment of customer funds by FCMs and DCOs and another final rule codifying the no-action position in CFTC staff letter 19-17 regarding separate account treatment by FCMs. The CFTC also has suggestions on your New Year's resolution.

New Developments

- **Customer Advisory: Avoiding Fraud May be Your Best Resolution.** A new CFTC [customer advisory](#) suggests adding “spotting scams” to your list of New Year’s resolutions. The Office of Customer Education and Outreach’s Avoiding Fraud May be Your Best Resolution says that with scammers robbing billions of dollars from Americans through relationship investment scams, resolving to be careful about who you trust online, staying informed, and learning all you can about trading risks are admirable 2025 resolutions. [NEW]
- **CFTC Approves Final Rule on Margin Adequacy, Treatment of Separate Accounts of a Customer by Futures Commission Merchants.** On December 20, 2024, the CFTC announced a [final rule](#) to implement requirements for futures commission merchants related to margin adequacy and the treatment of separate accounts of a customer. The rule finalizes the Commission’s proposal, published in the Federal Register in March, to codify the no-action position in CFTC staff letter 19-17 regarding separate account treatment. [NEW]
- **CFTC Approves Final Rule Regarding Safeguarding and Investment of Customer Funds.** On December 17, the CFTC announced that it approved a [final rule](#) amending the CFTC’s regulations that govern how futures commission merchants and derivatives

clearing organizations safeguard and invest customer funds held for the benefit of customers engaging in futures, foreign futures, and cleared swaps transactions. The amendments revise the list of permitted investments in CFTC Regulation 1.25 and make other related changes and specifications. The amendments also eliminate the CFTC requirement that an FCM deposit customer funds with depositories that provide the CFTC with read-only electronic access to such accounts. The compliance date for the revisions is 30 days after the final rule is published in the Federal Register, except for the revisions to the Segregation Investment Detail Reports (“SIDR”) specified in CFTC Regulations 1.32, 22.2(g)(5), and 30.7(l)(5), and the revisions to the customer risk disclosure statement required under CFTC Regulation 1.55. The compliance date for the revisions to the SIDR and the risk disclosure statement is March 31, 2025. [NEW]

- **CFTC Commissioner Kristin N. Johnson Announces Reports and Recommendations Advanced by MRAC in 2024.** The Market Risk Advisory Committee (“MRAC”) held a public meeting Dec. 10 during which the MRAC adopted three sets of recommendations for the CFTC’s consideration. The reports and accompanying recommendations address (i) U.S. Treasury markets with a focus on effective risk management practices for the cash-futures basis trade, (ii) modernization of regulation governing cyber resilience and critical third-party service providers for central counterparties, and (iii) the potential benefits and limitations of formally adopting obligations to employ legal entity identifiers for beneficial account holders of certain intermediaries. Commissioner Johnson also [announced](#) that Danielle Abada, Christopher Lamb and Nita Somasundaram have joined her staff [NEW]
- **CFTC Grants QC Clearing LLC DCO Registration.** On December 17, 2024, the CFTC [announced](#) that it issued QC Clearing LLC an Order of Registration as a derivatives clearing organization under the Commodity Exchange Act. QC Clearing LLC permitted to clear, in its capacity as a DCO, fully collateralized positions in futures contracts, options on futures contracts, and swaps. [NEW]
- **CFTC Staff Issues Advisory Regarding Form 304 Submission Format Beginning January 15, 2025.** On December 12, the CFTC Division of Market Oversight issued an advisory notifying all merchants and dealers of cotton holding or controlling positions for future delivery in cotton (traders) that beginning next year they must submit the regulatory filing identified as “Form 304” through the CFTC’s online filings portal. The advisory notes that all traders who are subject to CFTC Regulation 17 CFR 19.00(a) beginning January 15, 2025, Form 304 must be submitted through the CFTC’s online filings portal, which has been updated for traders’ use. Form 304 should continue to be submitted via email through January 14, 2025.
- **CFTC Staff Issues Advisory Related to the Use of Artificial Intelligence by CFTC-Registered Entities and Registrants.** On December 5, the CFTC’s Divisions of Clearing and Risk, Data, Market Oversight, and Market Participants issued a [staff advisory](#) on the use of artificial intelligence in CFTC-regulated markets by registered entities and registrants. The advisory is intended to remind CFTC-regulated entities of their obligations under the Commodity Exchange Act and the CFTC’s regulations as these entities begin to implement AI. CFTC staff noted that it is closely tracking the development of AI technology and AI’s potential benefits and risks and that it values its

ongoing dialogue with CFTC-regulated entities and intends to monitor these entities' use of AI as part of the agency's routine oversight activities. According to the CFTC, the advisory is informed, in part, by public comments received in response to the staff's January 25, 2024 [Request for Comment on AI](#).

- **CFTC Releases FY 2024 Enforcement Results.** On December 4, the CFTC announced record monetary relief of over \$17.1 billion for fiscal year 2024. With the resolution of digital asset cases that resulted in the agency's largest recovery ever, this record amount included \$2.6 billion in civil monetary penalties and \$14.5 billion in disgorgement and restitution. In FY 2024, the agency brought 58 new actions including, in the CFTC's words, precedent-setting digital asset commodities cases, its first actions addressing fraud in voluntary carbon credit markets, complex manipulation cases in various markets, and significant compliance cases – including its largest compliance case ever. The CFTC also said that it continued to vigorously litigate pending actions, resulting in significant litigation victories and recoveries.

New Developments Outside the U.S.

- **ESMA Consults on the Internal Control Framework for Some of its Supervised Entities.** On December 19, ESMA launched a [consultation](#) on draft Guidelines related to the Internal Control Framework for some of its supervised entities. ESMA said that the proposed draft Guidelines build on the Internal Control Guidelines currently in place for Credit Rating Agencies and extend them to include also Benchmark Administrators, and Market Transparency Infrastructures (Trade Repositories, Data Reporting Services Providers and Securitization Repositories). The draft Guidelines outline ESMA's expectations for the components and characteristics of an effective internal control system, intended to ensure: a strong framework, detailing the internal control environment and informational aspects, and effective internal control functions, including compliance, risk management, and internal audit. The draft Guidelines also explain how ESMA applies proportionality in its expectations regarding the internal controls for a supervised entity. According to ESMA, the consultation is primarily aimed at ESMA supervised entities and prospective applicants for ESMA supervision. [NEW]
- **ESMA Releases Last Policy Documents to Get Ready for MiCA.** On December 17, ESMA published its [last package of final reports](#) containing Regulatory Technical Standards and guidelines ahead of the full entry into application of the Markets in Crypto Assets Regulation. Specifically, the package includes Regulatory Technical Standards on market abuse and guidelines on reverse solicitation, suitability, crypto-asset transfer services, qualification of crypto-assets as financial instruments and maintenance of systems and security access protocols. [NEW]
- **ESMA Consults on Proposals to Digitalize Sustainability and Financial Disclosures.** On December 13, ESMA published a [Consultation Paper](#) seeking stakeholders' views on how the European Single Electronic Format can be applied to sustainability reporting. The

proposals also aim to ease the burden associated with financial reporting. Interested stakeholders are invited to submit their feedback by March 31, 2025.

- **ESMA Consults on Open-Ended Loan Originating Alternative Investment Funds.** On December 12, ESMA published a [consultation paper](#) on draft regulatory technical standards on open-ended loan originating Alternative Investment Funds (“AIFs”) under the revised Alternative Investment Fund Managers Directive (“AIFMD”). AIFMD review has introduced some harmonized rules on loan originating funds. The goal of these rules is to provide a common implementing framework by determining the elements and factors that Alternative Investment Fund Managers need to consider when making the demonstration to their Competent Authorities that the loan originated AIFs they manage can be open-ended.
- **ESMA Consults on Technical Advice on Listing Act Implications.** On December 12, ESMA launched a [consultation](#) to gather feedback following changes to the Market Abuse Regulation (“MAR”) and Market in Financial Instruments Directive II (“MiFID II”) introduced by the Listing Act. Regarding MAR, ESMA is inviting feedback on: a non-exhaustive list of the protracted process and the relevant moment of disclosure of the relevant inside information (together with some principles to identify the moment of disclosure for protracted not listed processes); a non-exhaustive list of examples where there is a contrast between the inside information to be delayed and the latest public announcement by the issuer; and a methodology and preliminary results for identifying trading venues with a significant cross-border dimension, for the purposes of establishing a Cross Market Order Book Mechanism. Regarding MiFID II, ESMA’s proposals cover: a systematic review of the relevant provisions in Commission Delegated Regulation 2017/565 to ensure that a Multilateral Trading Facility (“MTF”) (or a segment of it) to be registered as small and medium-sized enterprises growth market complies with the relevant requirements in the revised MiFID II; and some conditions to meet the registration requirements for a segment of an MTF, as specified in the revised MiFID II.
- **ESAs Provide Guidelines to Facilitate Consistency in the Regulatory Classification of Crypto-Assets by Industry and Supervisors.** On December 10, the European Supervisory Authorities (the “ESAs”) published [joint Guidelines](#) intended to facilitate consistency in the regulatory classification of crypto-assets under Markets in Crypto Asset Regulation. The Guidelines include a standardized test to promote a common approach to classification as well as templates market participants should use when communicating to supervisors the regulatory classification of a crypto-asset.
- **IOSCO Publishes Final Report on Regulatory Implications and Good Practices on the Evolution of Market Structures.** On November 29, IOSCO published its [Final Report on the Evolution in the Operation, Governance, and Business Models of Exchanges](#). According to IOSCO, the Final Report addresses significant changes in exchange business models and market structures, highlighting the impact of increased competition, technological advancements, and cross-border activity on exchanges. Additionally, it outlines a set of six good practices for regulators to consider in the supervision of exchanges that cover three key areas: (1) Organization of Exchanges and

Exchange Groups (2) Supervision of Exchanges and Trading Venues within Exchange Groups and (3) Supervision of Multinational Exchange Groups.

New Industry-Led Developments

- **FRTB Implementation Challenges: Capitalization of Funds.** On December 13, ISDA published a second [whitepaper](#) on the capitalization of equity investment in funds (“EIIFs”) under the Fundamental Review of the Trading Book (“FRTB”) framework. This paper builds upon an earlier ISDA publication in 2022 that highlighted the overly conservative capital requirements and operational complexities resulting from the proposed Basel III framework associated with EIIFs. Since then, several jurisdictions have implemented the FRTB (Canada and Japan), while others have finalized their FRTB rules (the EU and the UK) or are consulting on the final rules (the US). This topic continues to be a globally important issue for the industry, with many unresolved concerns related to the treatment of EIIFs.
- **ISDA Responds to HM Treasury on Financial Services Growth and Competitiveness Strategy.** On December 12, ISDA submitted its [response](#) to HM Treasury’s call for evidence on its financial services growth and competitiveness strategy. In the response, ISDA focused on innovation, technology, international partnerships and trade and sustainable finance. ISDA also urged the UK government to progress its review of markets and infrastructure regulation and retain its focus as a world leading host for central counterparties. [NEW]
- **Joint Associations Send Letter on UK CCP Equivalence and Recognition.** On December 12, ISDA and eleven other trade associations representing a broad group of market participants sent a [letter](#) to Commissioner Albuquerque requiring that the European Commission extends the equivalence decision for UK Central Counterparties in a non-time-limited manner and well in advance of March 31, 2025. The current time-limited equivalence decision is set to expire on June 30, 2025.
- **ISDA Publishes Paper on Compliance Requirements under MIFIR.** On December 9, ISDA published a [paper](#) that maps out an approach to post-trade transparency under the revised Markets in Financial Instruments Regulation for reporting single-name credit default swaps referenced to global systemically important banks, supporting meaningful transparency and implementation practicability.

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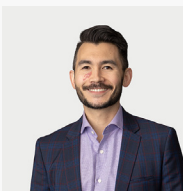
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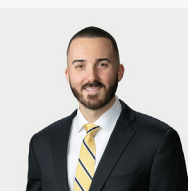
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