

Post-Election Outlook: Derivatives Regulatory Agenda

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Futures and Derivatives; CFTC

On November 8, 2016, American voters elected Republican Donald J. Trump as President. In addition, Republicans maintained control of the House of Representatives and the Senate. As the campaign rhetoric fades into the background over the coming weeks and months, the business of transitioning to a new administration will begin in earnest. The results of the election promise to have a significant impact on the regulatory agenda of the Commodity Futures Trading Commission (CFTC). Covington's Futures and Derivatives practice will be closely monitoring developments at the CFTC on an ongoing basis during this transition and stands ready to assist clients in navigating the new derivatives regulatory environment.

CFTC's Post-Election Regulatory Agenda

There remain several outstanding regulatory priorities for the CFTC. These include finalization of proposed rules on position limits, automated trading, and swap dealer capital requirements for non-banks. Several of these items had been anticipated to be completed by year's end. However, given the outcome of the election, we expect little regulatory movement until early next year. In fact, we expect that the Trump Administration Transition Team will soon be in discussions with the current CFTC Commissioners and staff in order to gather information on the current CFTC agenda. As a result, we would anticipate a hold on all pending regulatory actions. A larger issue for market participants to monitor is whether the Dodd-Frank Act will be repealed in its entirety and replaced with new legislation or whether the Dodd-Frank Act will be amended to rescind certain provisions. In short, it is early in the overall transition process, therefore the specific outcomes are unclear.

The Upcoming Republican-Led Commission: Re-Examination of Algorithmic Trading and Cross-Border Guidance

While the CFTC's regulatory actions are likely to be put on hold, we expect that Chairman Massad will step down following the inauguration and Commissioner J. Christopher Giancarlo, the lone Republican Commissioner, will become Acting Chair until such time as President Trump nominates, and the Senate confirms, a permanent Chair. It is possible that the Acting Chair (whether Commissioner Giancarlo or someone else) could become the permanent Chair. In addition to the Chair, there will be two additional Republican seats at the CFTC. President Obama recently nominated Christopher Brummer, a Democrat, and Brian Quintenz, a Republican, to become CFTC Commissioners. In late September 2016 the nominees were reported favorably out of the Senate Agriculture Committee, which permitted consideration by the full Senate. It is possible that Messrs. Quintenz and Brummer will receive support from President-elect Trump and become a Commissioner in the new year when the Administration is

in place. Market participants will also have to monitor the plans of the current Democrat Commissioners, Chairman Timothy Massad and Commissioner Sharon Bowen. It is possible there could be departures before the end of the year or in advance of the inauguration.

While the ultimate composition of the Commission will develop over time, the leadership by a Republican Chairman will have a significant impact on the CFTC's regulatory agenda. In particular, we note that Commissioner Giancarlo recently voiced [strong opposition](#) to the CFTC's supplemental Regulation Automated Trading ("Reg. AT") proposal. In particular, Commissioner Giancarlo criticized the Reg. AT proposal for allowing the CFTC to obtain the source code of market participants without a subpoena, arguing that this would "strip owners of intellectual property of due process of law;" that it would set a dangerous regulatory precedent; and, even, that it would be a possible violation of the Constitutional guarantee of freedom from unreasonable searches and seizures.

The concerns expressed by Commissioner Giancarlo in his opposition to proposed Reg. AT are consistent with a theme he has voiced throughout his term—steadfast support for technology and market innovation. Thus, under an Acting Chairman Giancarlo we would expect that the CFTC's regulatory agenda would begin to focus on ways that the agency could spur innovation and the use of technology in the derivatives markets, as well as removing what he perceives as existing regulatory barriers to innovation. For example, in a recent [speech](#) to the American Enterprise Institute, Commissioner Giancarlo stated that the CFTC was "stuck in a 20th century time warp" and that its "practices and culture are indifferent to today's financial technology revolution." Commissioner Giancarlo focused in particular on the CFTC's rules for swap execution facilities ("SEFs"), which he argued were "biased against human discretion and technological innovation."

Additionally, Commissioner Giancarlo has been critical of the CFTC's cross-border guidance and recently [stated](#), "I have been a critic of the Commission's 2013 over-expansive cross-border interpretative guidance and its avoidance of the rulemaking process to implement the sweeping policies contained therein." Specifically, Commissioner Giancarlo has been critical of CFTC staff cross-border guidance related to the CFTC's claim of jurisdiction over swaps between a non-U.S. swap dealer and a non-U.S. person when the swap is arranged, negotiated or executed by personnel of the non-U.S. swap dealer located in the U.S. Given the above, under the new Administration we expect a detailed examination of the cross-border guidance and future, significant rulemaking on this topic.

While there may not be significant CFTC rulemaking between now and President-elect Donald Trump's inauguration, there will be ongoing developments at the CFTC as it prepares for a transition to a new Administration. These changes will set the stage for the CFTC's regulatory agenda over the coming years.

Covington closely monitors CFTC developments in order to advise multiple market participants, including swap dealers, asset managers, hedge funds, commodity end-users, and trading and clearing platforms, on those developments with a diverse practice coverage. As the changes that will shape the derivatives regulatory landscape over the next year come into focus, we will be well-positioned to assist market participants in analyzing and evaluating the impact of the new CFTC agenda on their businesses.

If you have any questions concerning the material discussed in this client alert, please contact the following members of our Futures and Derivatives/CFTC practice:

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