

BROKER-DEALER

FINRA Issues Report on Implications of Blockchain

On January 18, the Financial Industry Regulatory Authority, responding to increased industry interest in distributed ledger technology (DLT) known as “Blockchain,” issued a report on the uses and potential implications of this technology in the securities industry.

The report provides an overview of DLT and its applications in various markets as well as discussing governance, operational structure and security concerns. The report also discusses regulatory challenges for broker-dealers, noting that a DLT network may create new ways to hold customer funds, impact a member firm’s net capital requirements, afford market participants the ability to develop and maintain certain records on the network itself, and alter clearance and settlement processes.

The report does not suggest new rules or guidelines, but instead seeks comments on the challenges associated with DLT and is intended to be an initial contribution to an ongoing dialogue with market participants.

The FINRA report is available [here](#).

DERIVATIVES

40 Days Left Until Compliance Date for Variation Margin Rules for Uncleared Swaps

As part of a global regulatory initiative, the United States, European Union, Canada, Switzerland, Japan, Hong Kong, Singapore and Australia have all adopted, or are in the process of adopting, rules (Margin Rules) that impose mandatory variation margin requirements on non-cleared swaps and, in some cases, non-cleared security-based swaps and FX derivatives (collectively, “Covered Trades”). Starting March 1, any entity that is a financial end user (FEU) will only be able to execute a Covered Trade with a US swap dealer if it has amended its swap documentation to comply with the requirements applicable to the dealer under the Margin Rules.

An FEU includes:

- banks, savings and loans and other similar entities;
- credit or lending entities, such as finance companies and money lenders;
- broker-dealers, investment companies and private funds;
- commodity pools, commodity pool operators (CPOs), commodity trading advisors (CTAs) and futures commission merchants (FCMs);
- ERISA plans;
- insurance companies;
- collective investment vehicles;
- proprietary traders; and
- foreign persons that would be any of the above if organized under US law.

What Does Each FEU Need to Do?

1. Each FEU will need to amend its collateral documentation with each of its swap dealer counterparties by March 1. If you have not yet been contacted by all your swap dealer counterparties, you should reach out to them to start a variation margin dialogue.
2. The amendment process starts with an exchange of information about the margin status of the FEU, which can be conveyed to counterparties via the Regulatory Margin Self-disclosure Letter published by ISDA, available [here](#).
3. Your current margin documentation can be amended using a bilateral amendment agreement provided by your swap dealer counterparty or by means of the 2016 Variation Margin Protocol published by ISDA. Information about the ISDA Variation Margin Protocol is available [here](#).

See “CFTC Grants Order to LCH” and “CFTC Proposes to Amend Access to Swap Data Requirements” in the CFTC Section.

CFTC

CFTC Grants Order to LCH

On January 13, the Commodity Futures Trading Commission issued an order authorizing LCH.Clearnet Limited (LCH), a CFTC-registered derivatives clearing organization (DCO), and its clearing members that are registered futures commission merchants to: (1) commingle in a cleared swaps customer account customer money, securities and property used to margin, secure or guarantee both futures and foreign futures (“futures”) and cleared swaps; and (2) portfolio margin such futures and cleared swaps, subject to the requirements of CFTC Regulation 39.13(g)(4). Regulation 39.13(b)(4) provides that a DCO may allow reductions in initial margin requirements provided the price risks with respect to such positions are significantly and reliably correlated.

For more information on the order, click [here](#).

CFTC Proposes to Amend Access to Swap Data Requirements

On January 13, the Commodity Futures Trading Commission approved for publication in the *Federal Register* proposed amendments to Part 49 of the CFTC’s regulations relating to access to swap data held by Swap Data Repositories (SDR). Among other revisions, the proposal: (1) eliminates the requirement that foreign and domestic authorities seeking access to SDR swap data first indemnify the CFTC and each SDR from which such authorities access swap data; (2) permits, subject to satisfying certain conditions, domestic regulators to access SDR swap data by entering into confidentiality arrangements with the CFTC, and other domestic authorities, and all foreign authorities to receive such swap data after being deemed “appropriate” by the CFTC.

The CFTC also approved for publication in the *Federal Register* proposed amendments to Part 3 (relating to registration) and Part 9 (relating to review of exchange disciplinary, access denial or other adverse actions) of the CFTC’s regulations. The proposed amendments integrate existing advisory guidance, incorporate swap execution facilities (SEFs), update provisions currently applicable to designated contract markets (DCMs) and require the publication of final disciplinary and access denial actions taken by the SEFs and DCMs on their exchange websites.

Comments on the proposed rules must be received within 60 days following publication of the proposed amendments in the *Federal Register*.

For more information on the proposed amendment, click [here](#).

CFTC’s Enforcement Division Issues New Advisories on Cooperation

On January 19, the Commodity Futures Trading Commission Division of Enforcement (“Division”) issued two new Enforcement Advisories outlining the factors the Division will consider in evaluating cooperation by individuals and companies in the Division’s investigations and enforcement actions. The advisory regarding companies updates an advisory last issued in 2007; the advisory regarding individuals is new. The advisories describe the factors that

the Division may consider, on a discretionary basis, when determining whether a company has cooperated, the quality of that cooperation and what credit, if any, should be awarded for such cooperation. Among other factors, the Division considers whether individuals and companies are truthful and fully cooperate in Division investigations and enforcement actions, including by self-reporting and providing early and material assistance to the Division.

For more information on the advisories, click [here](#).

EU DEVELOPMENTS

ESMA Publishes Briefing on MiFID II Technical Data Reporting Requirements

On January 13, the European Securities and Markets Authority (ESMA) published a briefing paper (Briefing Paper) summarizing technical data reporting requirements under the revised Markets in Financial Instruments Directive (MiFID II) and the associated Markets in Financial Instruments Regulation (MiFIR).

The Briefing Paper refers to the technical requirements and templates for data reporting, which ESMA published in October 2016 (four separate documents available [here](#), [here](#), [here](#) and [here](#)), and indicates the following dates for the start of data collection:

- By July 2017: ESMA plans to start the collection of instrument reference data from trading venues and systematic internalizers (Article 4 of the Market Abuse Regulation and Article 27 of MiFIR).
- By September 2017: ESMA plans to start the collection of data for transparency and double volume cap calculations from trading venues, approved publication arrangements, and consolidated tape providers (Article 22 of MiFIR).
- By January 3, 2018: national competent authorities plan to start the collection of transaction data from investment firms (Article 26 of MiFIR).

ESMA's Briefing Paper is available [here](#).

UK/BREXIT DEVELOPMENTS

UK Announces Brexit Negotiating Principles

On January 17, UK Prime Minister Theresa May laid out the UK government's negotiating principles for the United Kingdom's departure from the European Union, which heralds a new, more substantive phase of the Brexit process.

The Prime Minister's theme for the speech was the creation of a "stronger, fairer and global Britain" alongside a "new partnership" with the UK's EU allies. The balance of the speech was devoted to describing May's 12 key priorities in the upcoming negotiations, several of which are directly relevant for the financial markets. May also announced that both the House of Commons and the House of Lords will be given the opportunity to vote on the final deal with the European Union.

Of particular note for the financial markets, May stated that the UK government's economic priorities are twofold: (1) departure from the EU single market, to be replaced by a "bold and ambitious" free trade deal that would provide the "freest possible" trade in goods and services with the European Union; and (2) near-total departure from the EU customs union, to provide the United Kingdom with the ability to enter free trade agreements with other countries, including the United States, which would not be possible within the EU customs union (which negotiates as a bloc with third countries). However, the Prime Minister did suggest her preference for the United Kingdom to maintain tariff-free access to the European Union via another form of association to the EU customs union. The speech also confirmed the UK government's intention to end the jurisdiction of the European Court of Justice in the United Kingdom and to ensure that EU law and regulation that has accrued over time—referred to as the *acquis communautaire*—will be incorporated into UK domestic law prior to the United Kingdom's departure from the European Union.

In order to avoid any instability during the period immediately following Brexit, the Prime Minister proposed a “phased implementation” to the “new partnership” between the United Kingdom and the European Union, while expressly stating that an “unlimited transition” would not be acceptable. May noted that the specific phases and timing could proceed at variable speeds depending on the specific sector/area and according to what negotiators are able to achieve. This means, for example, that the transition period (if any) for financial services could proceed faster, or more slowly, than for immigration. The Prime Minister’s aim is to ensure a “smooth and orderly Brexit.”

The speech concluded with a warning to EU leaders that any attempt at a punitive Brexit deal would not be accepted by the UK government, which would prefer “no deal” to a “bad deal.” With “no deal,” the United Kingdom would cease to be an EU Member State two years following the date of the Article 50 notice of its intention to leave the European Union, with no transitional arrangements or ongoing obligations. The United Kingdom could then, as the Prime Minister suggested and other members of the UK government have previously stated, be free to lower its taxes, decrease regulation, and “change its economic model,” in a way to attract business and investment from the European Union.

For the financial markets, the Prime Minister’s speech provided some useful clarity that the United Kingdom will exit the EU’s single market and customs union, while leaving open the possibility of continued cross-border access by UK financial services firms (through new free trade and customs arrangements to be agreed between the United Kingdom and the European Union). May’s approach also would not hinder the potential application to the United Kingdom of the equivalence regimes in specific EU financial services legislation. However, the form that such final arrangements will take, and the specific services and firms that will benefit from continued cross-border access, will only be made clear after a lengthy negotiating process. In light of this continuing uncertainty and the time and resources required to shift business activities and personnel, some large financial institutions have indicated in the UK media that they will be deciding on their relocation arrangements soon. Some firms expect up to 20 percent of their London-based workforce to move into the European Union following Brexit.

The full text of the Prime Minister’s speech is available [here](#).

For additional coverage on financial and regulatory news, visit [Bridging the Week](#), authored by Katten's [Gary DeWaal](#).

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EU/UK/BREXIT DEVELOPMENTS

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