COMMODITY FUTURES TRADING COMMISSION

17 CFR Part 1

Recordkeeping

AGENCY: Commodity Futures Trading Commission.

ACTION: Proposed rules.

SUMMARY: The Commodity Futures Trading Commission (''CFTC'' or ''Commission'') is proposing to amend its Regulation 1.31 to maximize the cost-reduction and time-savings arising from technological developments in the area of electronic storage media while maintaining necessary safeguards to ensure the reliability of the recordkeeping process. Specifically, the Commission proposes to expand the category of required records for which an affected person may employ electronic storage media to meet the recordkeeping obligations imposed by the Commodity Exchange Act (''Act'' or ''CEA'') and Commission regulations. In addition, the Commission proposes to eliminate the current requirement that paper records eligible for transfer to micrographic storage media be maintained in hard copy form for two years. The Commission is also seeking comment on several recordkeeping-related issues.

DATES: Comments must be received on or before August 4, 1998.

ADDRESSES: Comments should be mailed to Jean A. Webb, Secretary, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW, Washington, DC 20581; transmitted by facsimile to (202) 418–5521; or transmitted electronically to (secretary@cftc.gov). Reference should be made to ''Recordkeeping''.

FOR FURTHER INFORMATION CONTACT: Edson G. Case, Counsel, or Robert B. Wasserman, Special Counsel, Division of Trading and Markets, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW, Washington, DC 20581. Telephone (202) 418–5430.

SUPPLEMENTARY INFORMATION:

I. Background

Commission Regulation 1.31 sets forth certain recordkeeping requirements imposed by the CEA or Commission regulations. For example, it mandates that record required to be kept by the Act or Commission regulations (''required records'') be maintained for a period of five years and be kept in a ''readily accessible'' manner for the first two years of this period. Regulation 1.31 also defines the rights of representatives of the Commission and Department of Justice to inspect and obtain copies of required records.[1]

Regulation 1.31 takes into account some technological advances in the development of recordkeeping systems. For example, it defines the circumstances under which a reproduction of a paper record on microfilm or microfiche may be substituted for the original paper record,[2] as well as the circumstances under which a computer, accounting machine or business machine generated record nay be transferred to and retained on optical disk media or microfilm/microfiche media.[3] It also imposes special inspection-related requirements for persons who choose to maintain their records on these media.[4]

The Commission has recently undertaken a series of steps to facilitate the use of electronic media technology where adequate measures exist to safeguard regulatory interests.[5] Various issues implicating the Commission's recordkeeping requirements under Regulation 1.31 have arisen in the context of these Commission initiatives. Indeed, in a February 20, 1997 Federal Register release, the Commission specifically acknowledged that ''it may be necessary to amend Regulation 1.31 to account for further technological developments.''[6]

In recognition of both the need for interim relief and the number of Commission registrants that are also subject to the recordkeeping requirements of the Securities and Exchange Commission (''SEC''), the Commission has had occasion to rely on the recordkeeping rules the SEC adopted in February 1997.[7] For example, in August 1997, the Commission adopted revisions to Part 4 addressing the use of electronic media by commodity pool operators (''CPOs'') and commodity trading advisors (''CTAs'') for delivery of disclosure documents and other materials.[8] Several of the comments during this rulemaking raised questions about the practicality of the Commission's current recordkeeping requirements in the context of electronic media. In response to these comments, the Commission permitted CPOs and CTAs to use the guidelines set forth in the SEC's rulemaking in lieu of the requirements of Regulation 1.31.[9] The Commission took this step ''[t]o facilitate CPOs' and CTAs' use of electronic media when possible and to avoid imposing duplicative or inconsistent requirements on registrants who may also be registered with the SEC. . . .''[10]

Consistent with these goals, experience with registrants' maintaining records in accordance with the SEC's rules, and a commitment to maximizing the cost-reduction and time-savings arising from technological developments in the area of electronic

[1] For example, Regulation 1.31(a) provides that all required records shall be open to inspection by such representatives and imposes on the person required to maintain the records a duty to provide a copy (at the person's expense) of any required record requested by such representatives. In addition, the regulation states that the person shall provide all copies or originals ''promptly.''

[2] The regulation requires that all paper required records be maintained in hard-copy form for the first two years of the mandated five-year period, after which they may be transferred to microfilm and microfiche, except for trading cards and written customers orders, which must be maintained in hard-copy form and for the full five-year period.

[3] The regulation permits immediate transfer of computer or machine generated records to microfilm/microfiche media and permits immediate transfer of computer generated records to defined class of optical storage media.

[4] For Example, persons maintaining records in these media must maintain indexes of the records as well as facilities that permit representatives of the Commission and the Department of Justice to view and obtain hard copies of the records immediately. For records stored on the specified optical storage media, Regulation 1.31(c)(1)(iii) also mandates that a copy of each record be immediately provided ''on Commission compatible machine-readable media as defined in [Commission Regulation] 15.00(1) . . . .''

[5] *See, e.g.,* 62 FR 39104 (July 22, 1997) (interpreting Commission requirements affecting the use of electronic media by commodity pool operators (''CPOs'') and commodity trading advisors (''CTAs'') and amending Part 4 of the Commission's Rules in light of the interpretion); 62 FR 31507 (June 10, 1997) (issuing guidance regarding a futures commission merchant's (''FCM's'') electronic delivery of confirmation, purchase-and-sale, and monthly statements to customers and the related recordkeeping requirements); 62 FR 18265 (April 15, 1997) (adopting a voluntary program for CPOs and CTAs to use electronic means to file disclosure with the Commission); 62 FR 10441 (March 7, 1997) (providing for use of personal identification numbers for FCMs and introducing brokers (''IBs'') that use electronic means to file attested financial reports with the Commission); 62 FR 7675 (February 20, 1997) (permitting the use of electronic records of customer orders generated by an electronic order-routing system).

[6] 62 FR 7677, n. 26.

[7] 62 FR 6469. The SEC's rulemaking involved reporting requirements for brokers or dealers under the Securities Exchange Act of 1934.

[8] 62 FR 39104.

[9] The Commission adopted a similar approach in its advisory permitting FCMs to deliver confirmations, purchase and sale statements, and monthly statements electronically. 62 FR 31507 (June 10, 1997), and its advisory concerning compliance with the ''written'' record requirements of Commission Regulations 1.35. 62 FR 7675 (February 20, 1997).

[10] 62 FR 39112. The Commission's concern about the regulatory cost imposed on dual registrants is consistent with its traditional focus on minimizing unnecessary regulatory costs. For example, the Commission has adopted several rules that permit dual-registrant FCMs to fulfill Commission regulatory requirements in the same manner they fulfill SEC regulatory requirements. *See, e.g.,* Commission Rules 1.10(h), 1.12(b)(4), 1.14(b)(1), 1.15(d)(1), 1.16(c)(5), 1.17(a)(1)(ii)(C), 1.18(a), 1.52(a).

storage media while maintaining necessary safeguards to assure the reliability of the recordkeeping process, the Commission is proposing amendments to Regulation 1.31.

II. Discussion

The proposed rules would make several changes to the current requirements of Regulation 1.31. The proposed rules would shift the Commission's approach to recordkeeping technology from the current rule's focused specification of a particular class of optical disk or micrographic media to a more generic, performance-based approach to the definition of permissible technology. As a result, persons subject to the Commission's recordkeeping requirements would have more freedom to take advantage of technological advances and to tailor their recordkeeping systems to individual business needs. The proposed rules would also expand the class of required records that may be maintained on micrographic or electronic storage media for the full five-year period. The Commission anticipates that this change will permit the type of simplification and streamlining of recordkeeping systems likely to result in both a reduction in costs and improvements in system reliability. The Commission also anticipates that the proposed rules will foster improvements in the security and availability of required records. For example, the proposed rules would require that there be a duplicate copy of all records maintained on micrographic or electronic storage media and that the duplicate be stored at a location separate from the original.[11] As a result, incidents of loss of access to required records due to fire, flood, or other catastrophic circumstances should be reduced to a minimum.[12] The proposed regulation would also create a procedure that should allow the Commission to obtain access to required records maintained on electronic storage media even if the owner of the records has ceased doing business and, despite Commission regulations,[13] cannot be located.

A. Definitions of Micrographic and Electronic Storage Median

The proposed rules would include new definitions of both micrographic media and electronic storage media. The former definition would include microfilm and microfiche, which are permitted under the current regulation, but would open the definition to additional developments in this area by including ''any similar medium.'' The latter definition would extend to any digital storage system that meets four general criteria: (1) it preserves records exclusively in a non-rewritable, non-erasable format; (2) it verifies automatically the quality and accuracy of the recording process; (3) it serializes [14] the units of storage media and creates a time-date record whenever information is placed on the storage media; and (4) it permits the immediate downloading of indexes and records maintained on the storage media to any of the media permitted by the regulation (paper, micrographic media or electronic media). These generic requirements (which establish performance criteria similar to those in the present rule) are designed to permit the use of the broadest range of available technology while maintaining safeguards necessary to assure both the reliability of the stored information and immediate access to the stored information by representatives of the Commission and the Department of Justice.[15]

B. Conditions on the Use of Micrographic and Electronic Storage Media

The proposed conditions on the use of micrographic and electronic storage media are intended to maintain the ease of access necessary to the Commission's regulatory interests and to ensure that the Commission's access will not be compromised by catastrophic events. Affected persons who wish to use these types of storage media must index all stored information and keep available facilities allowing for immediate production of both easily readable images of the stored records and easily readable hard-copy images. Affected persons must also waive any privilege, claim of confidentiality or other objection to disclosure of non-Commission-required information stored on the same individual medium (e.g., the same disk or sheet of microfiche) with Commission-required records. In addition, such persons must store a duplicate of each record, in any of the media acceptable under the regulation, as well as a duplicate of each index, at a location separate from the original.

C. Additional Conditions on the Use of Electronic Storage Media

The nature and capabilities of electronic storage media foster an efficient approach to record production that can benefit both the Commission and persons subject to Regulation 1.31's record-production requirements. The Commission is proposing to retain the current requirement that, upon request by an appropriate representative, persons maintaining required records on electronic storage media immediately provide copies of such records on Commission compatible machine-readable media (as defined by Commission Regulation 15.00(1)).[16]

The nature and capabilities of electronic storage media raise special concerns about the Commission's ability to detect both inadvertent errors during the transfer and storage process and intentional alteration of the stored record. To address these concerns, the Commission is proposing that persons who maintain documents on electronic storage media develop and maintain written operational procedures and controls (an ''audit system'') [17] designed to provide accountability over both the initial storage of data on the electronic storage media and the entry of any

[11] The proposal does not specify how ''separate'' the location of the original records must be from the location of the duplicate records. The Commission anticipates that persons required to maintain records will use their business judgment in selecting a location for the duplicate records that is sufficiently distant to make it unlikely that both sets of documents could be destroyed by a single catastrophic event (such as a fire or flood) but sufficiently close to ensure that duplicate records may be accessed and retrieved promptly should the original documents be destroyed.

[12] During the week of October 28, 1996, a fire destroyed a Chicago warehouse operated by Brambles Information Services. As a result, records that Commission registrants were required to maintain under Regulation 1.31 were damaged and destroyed, and the Commission developed a special procedure for the affected registrants to obtain relief from their obligations under that regulation. *See* Commission Advisory 96–62, [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,907 (December 18, 1996).

[13] *See* 17 C.F.R. 3.30(b), 3.33(b)(4).

[14] To ''serialize'' a unit of storage media (such as a disk or a trading ticket) is to assign it a unique, consecutive number so that (1) an additional, forged unit cannot be surreptitiously inserted and (2) a ''true'' unit cannot be surreptitiously removed.

[15] The Commission is not proposing an approval process for persons who wish to convert from their current storage format to a system that maintains records on electronic storage media. Prior to any conversion to an electronic storage system, however, an affected person must submit a representation to the Commission that the selected electronic storage system meets the requirements set forth in paragraph (b) of Regulation 1.31.

[16] The copies must use a format and coding structure (e.g., ASCII) specified in the request. ASCII is the American Standard Code For Information Interchange, a scheme for arranging bits (one or zero) in groupings of eight-bit ''bytes,'' each of which represents a character.

[17] The Commission is not specifying the contents of this audit system, but data regarding the inputting of records and changes to existing records will be a part of the system. Data must be captured systematically on a computer or in hard copy form. The Commission envisions that the identities of individuals actually inputting records and making particular changes, and the identity of both new documents created and documents changed, are the kind of information that must be collected either automatically or systematically.

subsequent change to such data.[18] Both the written procedures and the results of the audit system must be available to representatives of the Commission and the Department of Justice at all times for immediate examination and must be maintained for the time period applicable to the records stored on the electronic storage media.

The range of available electronic storage media raises concerns about the Commission's ability to access stored information when a person who maintains documents on electronic storage media fails to comply as required by Regulation 1.31. Paper records and records maintained on micrographic storage can usually be accessed and understood without specific cooperation from the originator. In contrast, electronically stored data may be difficult to access or understand without information concerning the format in which the data has been stored. To address this concern, the Commission is proposing that persons who maintain required records on electronic storage media take steps to ensure that the Commission has a continuous source of the information necessary to access the records and indexes stored on that media.[19] Such persons must either (1) maintain, keep current, and make available such information to representatives of the Commission and the Department of Justice or (2) place in escrow and keep current a copy of the necessary information.[20]

The issue of ready access takes on particular importance when electronic storage media are the sole media used to maintain required records. For example, if a recordkeeper ceases doing business and cannot be located, gaining access to records maintained solely on electronic storage media would be costly and time-consuming, if not particularly impossible.[21] To ensure access to records in the circumstances, the SEC's current rules requires that records be available through an alternative source whenever a recordkeeper maintains documents solely on electronic storage media. Specifically, those rules require that brokers and dealers using electronic storage media as their sole media to maintain require records enter into an arrangement with a third-party that has access to such persons' electronic storage media and the ability to download information from such media to any medium acceptable to the SEC. The third party must undertake to take reasonable steps to provide the SEC with access to the information contained on the recordkeeper's electronic storage media including, as appropriate, arrangements for the downloading of required records in a format designated by the SEC.

The Commission is proposing a similar requirement for persons required to maintain records under the Act or Commission regulations. The Commission invites comments regarding the likely cost of this requirement.[22] The Commission also invites comment on any practical alternative that will ensure access to the records of uncooperative recordkeepers without imposing undue costs on recordkeepers that cooperate in the manner contemplated by Regulation 1.31.

D. Retention of Trading Cards and Written Customer Orders

The Commission intends to maintain the current requirement that trading cards and written customer orders be retained in hard-copy form for the full five-year period. When the Commission considered issues related to the unique status of these records in 1993, there was a consensus that transferring these records to alternative media for storage was not common in the industry.[23] Moreover, the three futures exchanges that commented at that time agreed that electronic storage media should have limited application to trading cards and written customer orders.[24]

There have been significant changes in the industry since 1993, including an increase in order flow through electronic order routing systems.[25] Similar changes in the securities industry led to the SEC's 1997 decision to permit almost all handwritten records, including customer orders, to be maintained on either micrographic or electronic storage media.[26] The SEC acknowledged the need for caution in this area, however, and rested its decision largely on its conclusion that ''many of the larger broker-dealers no longer create traditional order tickets (with or without handwritten notations) because such broker-dealers enter most orders directly through electronic systems which automatically retain an electronic record of the trade entry.'' [27]

At the present time, electronic order routing in the futures industry is not as prevalent as in the securities industry. Moreover, the Commission has only limited experience with the transfer of written records to electronic storage media. Given these circumstances and the importance of trading cards and written order tickets to an effective

[18] Because an eligible electronic storage medium creates records that are non-rewritable and non-erasable, both the original input transaction and the correcting transaction will be retained.

[19] The proposal does not specify a list of information that the Commission will invariably consider ''necessary.'' However, the Commission envisions that the necessary information will include the physical and logical format of the electronic storage media, the file format of all different information types maintained on the electronic storage media, and any source code, related documentation, and other information necessary to access the records and indexes maintained on the electronic storage media. The term ''physical format'' refers to the physical characteristics of the media and the equipment from which the information was transferred to the media (e.g., a 3.5'' high-density diskette created on an IBM-compatible personal computer). The term ''logical format'' refers to the type and version of the data management software, such as a database management system (e.g., Oracle version 8) or file storage system (e.g., DOS file allocation table, Windows-NT file store (NTFS)). The term ''file format of all information types'' refers to record from format information, descriptions of data fields, and the relationships between fields and/or records. The term ''source code'' refers to a computer program in a format that can be understood by humans. Source code is read by a specialized program, known as a compiler, and converted into ''object code,'' which is the format in which the program is understood by a computer. Other information which may be necessary to access the records and indexes stored on electronic storage media might include password information required to access either the equipment or the information, or the type and version of the operating system used on the equipment which created the media (e.g., Solaris version 2.6).

[20] Escrow arrangements are a common feature of software licensing agreements. For example, in a ''source code escrow,'' the licensor deposits with an independent third party escrow company a copy of the software's sources code and system documentation and covenants to update the code and documentation as necessary. The escrow agreement describes in detail the situations which will trigger release by the escrow company to the licensee of the materials deposited in escrow. *See* D. Bender, ''Software Development, Licensing, and Protection: Strategies for Evolving Technology,'' 9 No. 1 J. Proprietary Rts. 9 (Jan. 1997).

[21] The level of difficulty would vary with the nature of the electronic storage system used and the availability of the information such as the physical and logical file format of the electronic storage media, the file format of all different information types maintained on the electronic storage media, and the source code and related documentation. While the proposed rule would requires that the listed information be kept available to the Commission, a recordkeeper which has ceased doing business and (in violation of Commission regulations) disappeared may also fail to meet this requirement.

[22] Because the conversion to an electronic storage system is voluntary, and the requirement at issue would only apply to persons which maintain some or all of their records solely on electronic storage media, the Commission expects that an affected person would only convert to a recordkeeping system based solely on electronic storage media when the cost of obtaining the services of a qualified third party is less than the cost of maintaining a duplicate hard copy of all required records. Given these circumstances, the Commission invites comment on both the cost of obtaining the services of a qualified third party and the cost of maintaining a duplicate hard copy of required records

[23] 58 FR 27465, 27466 (May 10, 1993).

[24] *Id.*

[25] *See generally* 62 FR 7675.

[26] 62 FR 6471.

[27] *Id.*

audit trail for trades, the Commission believes it would be premature to permit these records to be stored on either micrographic or electronic storage media.

The Commission proposes to clarify the description of the class of records that must be retained in hard copy form for the full five-year period. Currently, Regulation 1.31 refers to ''written *customer* orders'' required to be kept pursuant to Regulation 1.35(a–1)(1), (a–1)(2) and (d) (emphasis supplied). Written order tickets for trades initiated by persons who may not be regarded as customers under these provisions can plan an important role in an effective audit system. Regulation 1.35(a) currently requires future commission merchants, introducing brokers, and members of contract markets to retain ''all orders (filled, unfilled or canceled) * * *'' Given these circumstances, the Commission proposes that the class of records that must be retained in hard copy form for the full five-year period be clarified by referring to ''written orders'' rather than ''written customer orders.''

Regulation 1.31 also refers to ''trading cards'' in its description of the class of records that must be retained in hard copy form for the full five-year period. The Commission proposes to clarify this reference by also including documents on which trade information is originally recorded in writing. These documents fall within the class of ''original source documents'' that Commission Regulation 1.35(a) requires to be retained and produced. The purpose of this clarification is to ensure that the Commission has access to written hard copy documents necessary to assure an effective audit trail.

E. Related Issues for Comment

The Commission invites comment on the issues raised by its proposed amendments to Regulation 1.31. The Commission also seeks comments on several related issues. The first involves the scope of the duty to permit inspection imposed by Regulation 1.31. As noted above, subsection (a)(1) provides that all required records shall be ''readily accessible'' during the first two years of the five-year maintenance period. Subsection (a)(2) mandates that an affected person promptly provide (at the affected person's expense) a copy of any required record requested by a representative of the Commission or the Department of Justice.[28] Nothing in these subsections, however, specifies how ''readily accessible'' a record must be to ensure prompt production in response to a request by a representative of the Commission or the Department of Justice.

Subsections (b), (c), and (d) of Regulation 1.31 govern the use of eligible ''reproductions'' as substitutes for hard copy records. As discussed above, the current regulations provide that, under appropriate circumstances, reproductions on microfilm, microfiche and optical disk may be substituted for hard copy records. As one of the conditions for permitting such a substitution, subsection (c) requires that affected persons, among other things, have on their premises ''facilities for immediately producing complete, accurate and easily readable'' hard copy images of the required records. Again, nothing in this subsection specifies how ''readily accessible'' a record must be to ensure immediate production in response to a request by a representative of the Commission or the Department of Justice.

The regulatory history of Regulation 1.31 does provide limited guidance regarding the difference between the standard governing production under subsection (a)—promptly—and the standard governing production under subsections (b), (c), and (d)—immediately. The requirement that copies of eligible reproductions be provided ''immediately'' was inherited from regulations promulgated by the Commission's regulatory predecessors, the Department of Agriculture and the Commodity Exchange Commission.[29] Subsection (a)'s requirement that an original hard copy record (or a copy of the record) be provided ''promptly'' upon request was adopted by the Commission in January 1981.[30] The Commission had initially proposed to permit a representative of the Commission or Department of Justice to remove an original hard copy record for reproduction unless the person required to maintain the record provided a copy ''immediately.''[31] In amending the proposal to substitute the standard ''promptly,'' the Commission noted that, in some circumstances, hard copy records might not be ''readily accessible'' for the final three years of the five-year storage period. The Commission acknowledged that this factor should be taken into account in formulating an appropriate standard and explained that, in such circumstances, production would be deemed prompt if the affected person ''retrieve[d] the documents requested as expeditiously as is reasonable in light of the circumstances.''[32] The Commission also noted that the extent and nature of a document request could be appropriate factors in assessing the promptness of a production, explaining that:

> The recordkeeper is obligated by this requirement to furnish a copy of the original of a book or record as expeditiously as reasonably can be expected. This modification is not intended to permit any person to avoid the responsibility to provide any member of the Commission staff with prompt, complete access to any books and records required to be maintained. Rather, it is a recognition that in practice a requirement to furnish copies immediately in all instances, depending upon the extent or nature of a staff request, could impose an unwarranted burden upon the recordkeeper.[33]

Finally, the Commission specifically stated that the adoption of the ''promptly'' standard in subsection (a) did not affect a ''recordkeeper's obligation under [subsection (c)] immediately to provide a 'facsimile enlargement' of any records kept on microfilm as permitted by Rule 1.31.''[34]

In a letter addressing technology issues facing the futures industry, the National Futures Association (''NFA'') has recommended that the Commission eliminate the timing standards from subsections (b), (c), and (d) of Regulation 1.31 and substitute a general standard providing that an affected person must be able to retrieve required records in a usable form by the next business day. Under this definition of ''readily accessible,'' production of both hard copy documents and eligible reproductions would be deemed prompt if copies were provided on the business day following the affected person's receipt of a request. In addition, NFA requests that the facility and equipment-related conditions subsections (c) and (d) impose on the substitution of eligible reproductions for hard copy records be limited to the two years when the original records must be readily accessible.

NFA proposes a uniform standard which would eliminate the distinction in the existing regulation between records maintained in hard copy and those maintained in electronic or micrographic media. The regulatory history discussed above shows that, in establishing production requirements under regulation 1.31, the Commission always has distinguished between records maintained in hard copy form and records maintained in electronic or

[28] In the alternative, the regulation provides that the affected person may promptly provide the original book or record for reproduction.

[29] *See generally* 41 FR 3192 (Jan. 21, 1976).

[30] 46 FR 21 (Jan. 2, 1981).

[31] 43 FR 50699 (Oct. 31, 1978).

[32] 46 FR 21 n. 6.

[33] 46 FR 21 (footnote omitted).

[34] 46 FR 21 n. 6.

micrographic format by requiring ''prompt'' production of hard copies and ''immediate'' production of copies of electronic and micrographic records. This distinction recognizes that the reduced space and storage requirements for electronic and micrographic records, as compared with hard copy records, enable recordkeepers to keep such required records on their premises, rather than in a separate storage facility, and accordingly, to make immediate production of such records upon request of a representative of the Commission or the Department of Justice.

Indeed, electronic recordkeeping technology continues to improve, enhancing the ability of registrants to meet their recordkeeping obligations, while further reducing their costs. Thus, it may remain appropriate to impose different production standards for hard copy records and electronic or micrographic records. Similarly, it may remain appropriate to require immediate production of electronic records, rather than next day production, acknowledging the technological improvements that make compliance with that standard reasonable.

Moreover, the Commission is unaware of any practical problems arising out of the production standards currently set forth in Regulation 1.31. Nevertheless, the Commission invites comment on NFA's recommendation, with particular attention to the existence of such problems, the benefits that might be incident to a uniform standard and how such a uniform standard could be implemented without compromising the Commission's regulatory interest in expeditious production of required records.

NFA's letter also raises questions about current Regulation 1.31's selective treatment of security/integrity issues raised by records maintained on electronic storage media. NFA correctly notes that current Regulation 1.31 does not include any requirements for the security/integrity of paper records, but has fairly detailed requirements for records stored on optical disks.[35] It recommends that the Commission move to a unified approach that mandates that all affected persons have and enforce reasonable procedures to keep their records from being altered or destroyed.

The Commission agrees that all affected persons must have and enforce procedures to keep their records from being altered or destroyed. Even apart from regulatory duties, maintenance of such a system serves important business interests of Commission registrants. As a regulatory duty, it is implicit in registrants' duty to supervise pursuant to Commission Regulation 166.3.[36] The Commission solicits comment on whether Regulation 1.31 could be improved by specifying the nature of this duty in the context of records maintained in hard copy form or on micrographic media.

The Commission believes that it is important that Regulation 1.31 take into account the special security/integrity issues raised by electronic storage media. Given the variety of electronic storage systems available and the pace of technological change in such systems, the Commission believes that it is prudent to require that persons who utilize such systems meet specific security/integrity standards, at least until the Commission gains more experience with such systems. The Commission solicits comment on whether the security/integrity standards in the proposed amendments to Regulation 1.31 can be made more practical or cost-effective while serving the Commission's regulatory interest in the maintenance of secure and accurate records.

Finally, NFA's letter raises an issue arising out of the Commission's February 1997 advisory on alternatives for complying with the written record requirements of Commission Regulation 1.35. In that advisory's discussion of electronic order-routing systems, the Commission referred to several ''no-action'' letters issued by the Commission's Division of Trading and Markets (''Division''). Those letters, in turn, discussed the capacity of particular electronic order-routing systems to capture the time a particular order was executed.[37] When the Commission described the general criteria for systems covered by the advisory in the latter portion of the document, it made the following statement:

> All order-related times required under Commission Regulation 1.35, as well as the times for all modifications, are to be captured to the highest level of precision achievable by the operating system. In this regard, the Commission's experience is that these systems have the capability, at a minimum, to capture times to the second. Therefore, the Commission is requiring that such times must be accurate at least to the second.[38]

In its conclusion, the Commission's advisory again described the time an eligible system should capture as ''at least to the second.''[39]

In its letter, NFA notes that this guidance does not sufficiently specify the appropriate increment of time a registrant's system must capture. It recommends that the Commission determine the appropriate increment of time all electronic time-recording systems should meet and apply this increment without regard to the particular system's capacity. In this regard, NFA contends that the regulatory benefit to mandating more precise time-stamping diminishes as the time increment approaches a fraction of a second.

The Commission intends that electronic time-recording systems covered by the advisory meet a one-second performance standard. However, for business-related reasons, affected persons may choose to operate systems that capture times at a more-refined level. If an affected person does operate its system in a manner that captures time increments of less than a second, it must make that information available at the request of a representative of the Commission or the Department of Justice. Put simply, an affected person may not fulfill its recordkeeping duties by providing the Commission with timing data less refined than the data its system has actually captured.

While the Commission believes this clarification addresses the issue raised by NFA, comment is invited on the role system capacity should play in assessing an affected person's recordkeeping responsibilities under the Act and Commission regulations.

III. Related Matters

A. Regulatory Flexibility Act

The Regulatory Flexibility Act (''RFA''), 5 U.S.C. § 601, *et seq.*, 611,

[35] The Commission addressed the security/integrity issue when it amended Rule 1.31 in 1993. The Commission explained that: The Commission's concern in this area relates to the trustworthiness of documents that may be relied upon by the Commission in conducting investigations and entered into evidence in administrative and judicial proceedings. In this respect, microfilm records are considered trustworthy, since the image cannot be readily altered and firms use documented procedures that are performed in the ordinary course of business. The Commission believes under specified conditions, optical disk storage can be as trustworthy as microfilm and paper records. 58 FR 27460.

[36] Regulation 166.3 requires each Commission registrant other than associated persons with no supervisory duties to diligently supervise the ''handling by its partners, officers, employees and agents (or persons occupying a similar status or performing a similar function) of * * * all * * * activities of its partners, officers, employees and agents (or persons occupying a similar status or performing a similar function) relating to its business as a Commission registrant.''

[37] Commission Regulation 1.35 requires that written customer orders be time-stamped with the date and time ''to the nearest minute.'' In this regard, the Division's no-action letters for two specific electronic order-routing systems noted that the systems had the capacity to capture execution times to the nearest second.

[38] 62 FR 7677.

[39] 62 FR 7678.

requires that, in adopting rules and regulations, all federal agencies consider their impact on small entities. In accordance with Section 601(3) of the RFA, the Commission published a ''Policy Statement of Definitions of Small Entities for Purposes of the Regulatory Flexibility Act,'' 47 FR 18618 (Apr. 30, 1982). In that statement,[40] the Commission indicated that some classes of persons were excluded from the definition of small entities. These include: futures commission merchants registered or required to be registered; floor brokers employed by registered futures commission merchants; commodity pool operators registered or required to be registered and large traders in the futures market. The Commission considers other entities to be small under particular facts and circumstances. These may include: futures commission merchants exempt from registration; commodity pool operators exempt from registration; introducing brokers; floor brokers not employed by futures commission merchants; floor traders and commodity trading advisors. Because the rules discussed herein will affect the full spectrum of Commission registrants, it is likely that small entities within the meaning of the RFA will be affected.

The proposed regulation amendments would generally expand the category of record storage systems permissible under the Commission's rules. The Commission anticipates that, if the proposed rules are adopted, small entities will have more freedom to tailor their record storage systems to the overall needs of their businesses. For example, the proposed rules would have no impact on a small entity that chooses to maintain a paper-based record storage system. For a small entity that chooses to use micrographic storage media for its record storage system, the proposed rules would permit the small entity to take advantage of technological advances. The only additional cost would be that of creating a duplicate record and storing it at a location separate from the original record. The bulk of this cost could be avoided by moving the hard copies of the records transferred to micrographic media to a separate location.

For a small entity that chooses to use electronic storage media, the proposed regulation would eliminate the current rule's requirement that the small entity use a limited class of optical storage technology. This change would permit small entities to select electronic storage systems that may be less costly and simpler to manage. The proposed rules would impose limited additional costs on small entities that use electronic storage technology. The new costs would include requirements that the affected person: (1) provide a representation that the system meets pertinent regulatory requirements prior to converting to an electronic storage system; (2) create a duplicate of both required records and an index of those records, and maintain the duplicate at a separate location; (3) create and maintain an audit system for transferring records to electronic storage media; (4) take steps to ensure Commission access to information necessary to download records from the electronic storage media; and (5) provide an independent source for the downloading of records that are maintained solely on electronic storage media. The Commission anticipates that small entities will not convert their recordkeeping systems to electronic storage media unless the accompanying costs are outweighed by the financial savings and operational efficiency that would result from the change to electronic storage media.

The Chairperson, on behalf of the Commission, hereby certifies, pursuant to 5 U.S.C. 605(b), that the action taken herein will not have a significant economic impact on a substantial number of small entities.

B. Paperwork Reduction Act

When publishing proposed rules, the Paperwork Reduction Act of 1995[41] (''PRA'') imposes certain requirements on federal agencies (including the Commission) in connection with their conducting or sponsoring any collection of information as defined by the PRA. In compliance with the PRA, the Commission through this rule proposal, solicits comments to:

(1) evaluate whether the proposed collection of information is necessary for the proper performance of the functions of the agency, including the validity of the methodology and assumptions used; (2) evaluate the accuracy of the agency's estimate of the burden of the proposed collection of information, including the validity of the methodology and assumptions used; (3) enhance the quality, utility and clarity of the information to be collected; and (4) minimize the burden of the collection of information on those who are to respond, including through the use of appropriate automated, electronic, mechanical or other technological collection techniques or other forms of information technology (e.g., permitting electronic submission of responses.

The Commission has submitted this proposal and its associated information collection requirements to the Office of Management and Budget. The burden associated with this entire collection (3038–0022), including the proposed rule, is as follows:

Average burden hours per response: 3,551.89
Number of respondents: 15,682
Frequency of response: On occasion

The burden associated with this specific proposed rule, is as follows:

Average burden hours per response: 17.50
Number of respondents: 3412
Frequency of response: On occasion

Persons wishing to comment on the information that would be required by this proposal should contact the Desk Officer, CFTC, Office of Management and Budget, Room 10202, NEOB, Washington, DC 20503, (202) 395–7340. Copies of the information collection submission to OMB are available from the CFTC Clearance Officer, 1155 21st Street N.W., Washington DC 20581, (202) 418–5160.

List of Subjects in 17 CFR Part 1

Recordkeeping requirements.

Accordingly, 17 CFR part 1 is proposed to be amended as follows:

PART 1—GENERAL REGULATIONS UNDER THE COMMODITY EXCHANGE ACT

1. The authority citation for Part 1 continues to read as follows:

Authority: 7 U.S.C. 1a, 2, 2a, 4, 4a, 6, 6a, 6b, 6c, 6d, 6e, 6f, 6g, 6h, 6i, 6j, 6k, 6l, 6m, 6n, 6o, 6p, 7, 7a, 7b, 8, 9, 12, 12a, 12c, 13a, 13a–1, 16, 16a, 19, 21, 23, 24.

2. Section 1.31 is amended by revising paragraphs (b), (c), and (d) to read as follows:

§ 1.31 Books and records, keeping and inspection.

* * * * *

(b) Except as provided in paragraph (d) of this section, immediate reproductions on either ''micrographic media'' (as defined in paragraph (b)(1)(i) of this section) or ''electronic storage media'' (as defined in paragraph (b)(1)(ii) this section) may be kept in that form for the required time period under the conditions set forth in this paragraph (b).

(1) For purposes of this section:

(i) The term ''micrographic media'' means microfilm or microfiche or any similar medium.

[40] The Commission subsequently clarified some of the definitions. *See* 48 FR 35276 (Aug. 3, 1983); 55 FR 13550 (Apr. 11, 1990); 58 FR 40347 (Jul. 28, 1993).

[41] Pub. L. 104–13 (May 13, 1995).

(ii) The term ''electronic storage media'' means any digital storage medium or system that:

(A) Preserves the records exclusively in a non-rewritable, non-erasable format;

(B) Verifies automatically the quality and accuracy of the storage media recording process;

(C) Serializes the original and, if applicable, duplicate units of storage media and creates a time-date record for the required period of retention for the information placed on such electronic storage media; and

(D) Permits the immediate downloading of indexes and records preserved on the electronic storage media onto paper, microfilm, microfiche or other medium acceptable under this paragraph upon the request of representatives of the Commission or the Department of Justice.

(2) Persons who use either micrographic media or electronic storage media to maintain records in accordance with this section must:

(i) Have available at all times, for examination by representatives of the Commission or the Department of Justice, facilities for immediate, easily readable projection or production of micrographic media or electronic storage media images;

(ii) Be ready at all times to provide, and immediately provide at the expense of the person required to keep such records, any easily readable hard-copy image that representatives of the Commission or Department of Justice may request.

(iii) Waive any privilege, claim of confidentiality, or other objection to disclosure of non-Commission-required information stored on the same individual medium (e.g. the same disk or sheet of microfiche) as Commission-required records;

(iv) Store a duplicate of the record, in any medium acceptable under this section, at a location separate from the original for the period of time required for maintenance of the original; and

(v) Organize and maintain an accurate index of all information maintained on both the original and duplicate storage media such that:

(A) The location of any particular record stored on the media may be immediately ascertained;

(B) The index is available at all times for immediate examination by representatives of the Commission or the Department of Justice;

(C) A duplicate of the index is stored at a location separate from the original index; and

(D) Both the original index and the duplicate index are preserved for the time period required for the records included in the index.

(3) In addition to the conditions in paragraph (b)(2) of this section, persons using electronic storage media must:

(i) Be ready at all times to provide, and immediately provide at the expense of the person required to keep such records, copies of such records on such approved machine-readable media as defined in § 15.00(l) of this chapter which any representative of the Commission or the Department of Justice may request. Records must use a format and coding structure specified in the request.

(ii) Develop and maintain written operational procedures and controls (an ''audit system'') designed to provide accountability over both the initial entry of required records to the electronic storage media and the entry of each change made to any original or duplicate record maintained on the electronic storage media such that:

(A) The results of such audit system are available at all times for immediate examination by representatives of the Commission or the Department of Justice;

(B) The audit results are preserved for the time period required for the records maintained on the electronic storage media; and

(C) The written operational procedures and controls are available at all times for immediate examination by representatives of the Commission or the Department of Justice.

(iii) Either:

(A) Maintain, keep current, and make available at all times for immediate examination by representatives of the Commission or Department of Justice all information necessary to access records and indexes maintained on the electronic storage media; or

(B) Place in escrow and keep current a copy of the physical and logical format of the electronic storage media, the file format of all different information types maintained on the electronic storage media and the source code, documentation, and information necessary to access the records and indexes maintained on the electronic storage media.

(4) In addition to the foregoing conditions, any person who uses only electronic storage media to preserve some or all of its required records (''Electronic Recordkeeper'') shall, prior to the media's use, enter into an arrangement with at least one third party technical consultant (''Technical Consultant'') who has the technical and financial capability to perform the undertakings described in this paragraph (b)(4). The arrangement shall provide that the Technical Consultant will have access to and the ability to download information from the Electronic Recordkeeper's electronic storage media to any media to any medium acceptable under this section.

(i) The Technical Consultant must file with the Commission on undertaking in a form acceptable to the Commission, signed by the Technical Consultant or a person duly authorized by the Technical Consultant. An acceptable undertaking must include the following provision with respect to the Electronic Recordkeeper:

> With respect to any books and records maintained or preserved on behalf of the Recordkeeper, the undersigned hereby undertakes to furnish promptly to any representative of the United States Commodity Futures Trading Commission or the United States Department of Justice (the ''Representative''), upon reasonable request, such information as is deemed necessary by the Representative to download information kept on the Electronic Recordkeeper's electronic storage media to any medium acceptable under 17 CFR 1.31. The undersigned also undertakes to take reasonable steps to provide access to information contained on the Electronic Recordkeeper's electronic storage media, including, as appropriate, arrangements for the downloading of any record required to be maintained under the Commodity Exchange Act or the rules, regulations, or orders of the United States Commodity Futures Trading Commission, in a format acceptable to the Representative. Such arrangements will provide specifically that in the event the Electronic Recordkeeper fails to download a record into a readable format and after reasonable notice to the Electronic Recordkeeper, upon being provided with the appropriate electronic storage medium, the undersigned will undertake to do so, at no charge to the United States, as the Representative may request.

(c) Persons employing an electronic storage system shall provide a representation to the Commission prior to the initial use of the system. The representation shall be made by the person required to maintain the records, the storage system vendor, or another third party with appropriate expertise and shall state that the selected electronic storage system meets the requirements set forth in paragraph (b)(1)(ii) of this section. Persons employing an electronic storage system using media other than optical disk or CD–ROM technology shall so state. The representation shall be accompanied by the type of oath or affirmation described in § 1.10(d)(4) of this chapter.

(d) Trading cards, documents on which trade information is originally recorded in writing, and written orders required to be kept pursuant to § 1.35(a), (a–1)(1), (a–1)(2) and (d), must be

retained in hard-copy for the required time period.

Issued in Washington, DC on may 29, 1998 by the Commission.

Jean A. Webb,

Secretary of the Commission.

[FR Doc. 98–14805 Filed 6–4–98; 8:45 am]

BILLING CODE 6351–01–M

COMMODITY FUTURES TRADING COMMISSION

17 CFR Part 10

Rules of Practice; Proposed Amendments

AGENCY: Commodity Futures Trading Commission.

ACTION: Extension of comment period.

SUMMARY: On April 3, 1998, the Commission published in the **Federal Register** a notice requesting comments on proposed amendments to its Rules of Practice, which govern most adjudicatory proceedings brought under the Commodity Exchange Act, as amended, except for reparations actions. The original comment period expires on June 2, 1998. 63 FR 16453 (April 3, 1998). In a letter dated May 28, 1998, the Committee on Commodities and Futures Law of the New York State Bar Association requested an extension of the comment period. To assure that an adequate opportunity is provided for the submission of meaningful comments, the Commission has determined to extend the comment period by an additional thirty (30) days.

DATES: Comments must be received on or before July 2, 1998.

ADDRESSES: Comments on the proposed amendments should be sent to Jean A. Webb, Secretary, Commodity Futures Trading Commission, Three Lafayette Center, 1155 21st Street, NW., Washington, DC 20581. Comments may be sent by electronic mail to secretary@cftc.gov. Reference should be made to ''Proposed Amendments to the Rules of Practice.''

FOR FURTHER INFORMATION CONTACT: Stephen Mihans, Office of Chief Counsel, Division of Enforcement, at (202) 418–5399 or David Merrill, Office of Chief Counsel, at (202) 5120, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW., Washington, DC 20581.

Issued at Washington, DC, on this 1st day of June, 1998, by the Commodity Futures Trading Commission.

Jean A. Webb,

Secretary of the Commission.

[FR Doc. 98–14961 Filed 6–2–98; 2:33 pm]

BILLING CODE 6351–01–M

DEPARTMENT OF ENERGY

Federal Energy Regulatory Commission

18 CFR Ch. I

[Docket No. RM98–8–000]

Alternative Methods for Regulating Natural Gas Pipeline Facilities and Services on the Outer Continental Shelf; June 1, 1998

AGENCY: Federal Energy Regulatory Commission, DOE.

ACTION: Notice of inquiry.

SUMMARY: The Federal Energy Regulatory Commission is initiating an inquiry into alternatives to the Commission's recent methods of exercising its jurisdiction over natural gas pipeline facilities and services on the Outer Continental Shelf.

The goal of the notice of inquiry is to generate public comment that will assist the Commission in exploring possible alternatives to the application of the existing ''primary function'' test to offshore pipeline facilities—as well as possible complimentary and/or alternative modes of regulation under the Outer Continental Shelf Lands Act.

The notice of inquiry invites all interested persons to participate in the inquiry and to submit answers to several specific questions.

DATES: Written comments must be received on or before July 16, 1998; an original and 14 copies should be filed.

ADDRESSES: All comments should refer to Docket No. RM98–8–000 and should be addressed to: Office of the Secretary, Federal Energy Regulatory Commission, 888 First Street, NE, Washington, DC 20426.

FOR FURTHER INFORMATION CONTACT: Robert Wolfe, Office of the General Counsel, Federal Energy Regulatory Commission, 888 First Street, NE, Washington, DC 20426, (202) 208–2098.

SUPPLEMENTARY INFORMATION: In addition to publishing the full text of this document in the **Federal Register**, the Commission also provides all interested persons an opportunity to inspect or copy the contents of this document during normal business hours in the Public Reference Room at 888 First Street, NE, Room 2A, Washington, DC 20426.

The Commission Issuance Posting System (CIPS) provides access to the texts of formal documents issued by the Commission. CIPS can be accessed via Internet through FERC's Homepage (http://www.ferc.fed.us) using the CIPS Link or the Energy Information Online icon. The full text of this document will be available on CIPS in ASCII and WordPerfect 6.1 format. CIPS is also available through the Commission's electronic bulletin board service at no charge to the user and may be accessed using a personal computer with a modem by dialing 202–208–1397, if dialing locally, or 1–800–856–3920, if dialing long distance. To access CIPS, set your communications software to 19200, 14400, 12000, 9600, 7200, 4800, 2400, or 1200 bps, full duplex, no parity, 8 data bits and 1 stop bit. User assistance is available at 202–208–2474 or by E-mail to CipsMaster@FERC.fed.us.

This document is also available through the Commission's Records and Information Management System (RIMS), an electronic storage and retrieval system of documents submitted to and issued by the Commission after November 16, 1981. Documents from November 1995 to the present can be viewed and printed. RIMS is available in the Public Reference Room or remotely via Internet through FERC's Homepage using the RIMS link or the Energy Information Online icon. User assistance is available at 202–208–2222, or by E-mail to RimsMaster@FERC.fed.us.

Finally, the complete text on diskette in WordPerfect format may be purchased from the Commission's copy contractor, La Dorn System Corporation. La Dorn Systems Corporation is located in the Public Reference Room at 888 First Street, NE, Washington, DC 20426.

I. Introduction

In 1995, in response to heightened interest in Outer Continental Shelf (OCS) exploration and development, the Commission undertook a review of its OCS gathering policy through a notice of inquiry in Docket No. RM96–5–000. On February 28, 1996, the Commission issued a statement of policy respecting pipeline facilities on the OCS.[1] The policy statement concluded that facilities located in deep water (a depth of 200 meters or more) would be

[1] Gas Pipeline Facilities and Services on the Outer Continental Shelf—Issues related to the Commission's Jurisdiction Under the Natural Gas Act and the Outer Continental Shelf Land's Act (Policy Statement), 74 FERC ¶ 61,222 (Feb. 26, 1996).