BILLING CODE 6351-01

COMMODITY FUTURES TRADING COMMISSION

17 CFR Part 43

RIN: 3038-AD84

Rules Prohibiting the Aggregation of Orders to Satisfy Minimum Block Sizes or Cap Size Requirements, and Establishing Eligibility Requirements for Parties to Block Trades

AGENCY: Commodity Futures Trading Commission

ACTION: Notice of Proposed Rulemaking

SUMMARY: The Commodity Futures Trading Commission ("Commission") is issuing a notice of proposed rulemaking to add certain provisions to part 43 of the Commission's regulations pertaining to block trades in swap contracts. The provisions would: (i) prohibit the aggregation of orders for different trading accounts in order to satisfy the minimum block size or cap size requirements, except for orders aggregated by certain commodity trading advisors ("CTAs"), investment advisers and foreign persons (as described in this release), if such person has more than $25,000,000 in total assets under management ("AUM"); (ii) provide that parties to a block trade must individually qualify as eligible contract participants ("ECPs"), except where a designated contract market allows certain CTAs, investment advisers and foreign persons (as described in this release), to transact block trades for customers who are not ECPs, if such CTA, investment adviser or foreign person has more than $25,000,000 in total AUM; and (iii) require that persons transacting block trades on behalf of customers must receive prior written instruction or consent from the customer to do so.

DATES: Comments must be received on or before **[INSERT DATE 30 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER]**.

ADDRESSES: You may submit comments, identified by RIN number [TBD], by any of the following methods:

- The agency's website, at http://comments.cftc.gov. Follow the instructions for submitting comments through the website.
- Mail: David A. Stawick, Secretary of the Commission, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW, Washington, DC 20581.
- Hand Delivery/Courier: Same as mail above.
- Federal eRulemaking Portal: http://www.regulations.gov. Follow the instructions for submitting comments.

Please submit your comments using only one method.

All comments must be submitted in English, or if not, accompanied by an English translation. Comments will be posted as received to www.cftc.gov. You should submit only information that you wish to make available publicly. If you wish the Commission to consider information that you believe is exempt from disclosure under the Freedom of Information Act, a petition for confidential treatment of the exempt information may be submitted according to the procedures established in § 145.9 of the Commission's regulations.[1]

Commenters to this notice of proposed rulemaking are requested to refrain from providing comments with respect to the provisions in part 43 of the Commission's regulations that are beyond the scope of this notice of proposed rulemaking. The Commission only plans to address those comments that are responsive to the policies, merits and substance of the proposed provisions set forth in this notice of proposed rulemaking.

[1] See 17 CFR 145.9.

The Commission reserves the right, but shall have no obligation, to review, pre-screen, filter, redact, refuse or remove any or all of your submission from www.cftc.gov that it may deem to be inappropriate for publication, such as obscene language. All submissions that have been redacted or removed that contain comments on the merits of the rulemaking will be retained in the public comment file and will be considered as required under the Administrative Procedure Act and other applicable laws, and may be accessible under the Freedom of Information Act.

FOR FURTHER INFORMATION CONTACT: Nancy Markowitz, Deputy Director, Division of Market Oversight, 202-418-5453, nmarkowitz@cftc.gov; Nadia Zakir, Special Counsel, Division of Market Oversight, 202-418-5720, nzakir@cftc.gov; Laurie Gussow, Attorney-Advisor, 202-418-7623, lgussow@cftc.gov; George Pullen, Economist, Division of Market Oversight, 202-418-6709, gpullen@cftc.gov; Esen Onur, Economist, Office of the Chief Economist, 202- 418-6146, eonur@cftc.gov; or Herminio Castro, Counsel, Office of General Counsel, 202-418-6705, hcastro@cftc.gov, Commodity Futures Trading Commission, Three Lafayette Center, 1155 21st Street, NW, Washington, DC 20581.

SUPPLEMENTARY INFORMATION:

I. Background

A. The Dodd-Frank Act

On July 21, 2010, President Obama signed the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act").[2] Title VII of the Dodd-Frank Act[3] amended the

[2] See Pub. L. No. 111-203, 124 Stat. 1376 (2010).

[3] The short title of Title VII of the Dodd-Frank Act is the "Wall Street Transparency and Accountability Act of 2010."

Commodity Exchange Act ("CEA" or "Act")[4] to establish a comprehensive, new regulatory framework for swaps and security-based swaps. This legislation was enacted to reduce risk, increase transparency and promote market integrity within the financial system by, inter alia: (1) providing for the registration and comprehensive regulation of swap dealers ("SDs") and major swap participants ("MSPs"); (2) imposing mandatory clearing and trade execution requirements on standardized derivative products; (3) creating robust recordkeeping and real-time reporting regimes; and (4) enhancing the Commission's rulemaking and enforcement authorities with respect to, among others, all registered entities and intermediaries subject to the Commission's oversight.

Section 727 of the Dodd-Frank Act enacted section 2(a)(13) of the CEA, which authorizes and requires the Commission to promulgate regulations for the real-time public reporting of swap transaction and pricing data.[5] Among other things, sections 2(a)(13)(E)(ii) and (iii) of the CEA respectively require the Commission to prescribe regulations specifying "the criteria for determining what constitutes a large notional swap transaction (block trade) for particular markets and contracts" and "the appropriate time delay for reporting large notional swap transactions (block trades) to the public."[6]

B. The Initial Proposal

In order to implement the various statutory requirements imposed under section 2(a)(13) of the CEA, the Commission published an initial notice of proposed rulemaking on December 7,

[4] See 7 U.S.C. 1 et seq.

[5] See generally CEA section 2(a)(13), 7 U.S.C. 2(a)(13).

[6] See CEA sections 2(a)(13)(E)(ii) and (iii).

2010 (the "Initial Proposal").[7] As relevant to this notice of proposed rulemaking, the Initial Proposal proposed: (1) definitions for the terms "large notional off-facility swap" and "block trade";[8] (2) a method for determining the appropriate minimum block sizes for large notional off-facility swaps and block trades;[9] and (3) a framework for timely reporting of such transactions and trades.[10]

Among other requirements contained in the Initial Proposal, proposed § 43.5(b)(1) provided that eligible parties to a block trade (or large notional swap) must be ECPs,[11] except that a designated contract market ("DCM") may allow a CTA acting in an asset managerial capacity and registered pursuant to Section 4n of the Act, or a principal thereof, including any investment adviser who satisfies the criteria of § 4.7(a)(2)(v), or a foreign person performing a

---

[7] See Real-Time Public Reporting of Swap Transaction Data, 75 FR 76,139 (Dec. 7, 2010), as corrected in Real-Time Public Reporting of Swap Transaction Data Correction, 75 FR 76,930 (Dec. 10, 2010) ("Initial Proposal").

[8] The Initial Proposal defined the term "large notional swap". See proposed § 43.2(l), 75 FR 76,171. The Adopting Release finalized the term as "large notional off-facility swap", to denote, in relevant part, that the swap is not executed pursuant to SEF or DCM rules and procedures. See § 43.2, 77 FR 1182, 1244 (Jan. 9, 2012) ("Adopting Release"). Specifically, the Adopting Release defined the term as an "off-facility swap that has a notional or principal amount at or above the appropriate minimum block size applicable to such publicly reportable swap transaction and is not a block trade as defined in § 43.2 of the Commission's regulations." Id.

The final definition of "block trade" in the Adopting Release is similar to how that term was defined in the Initial Proposal. See proposed § 43.2(f), 75 FR 76,171. The Adopting Release defines the term "block trade" as a publicly reportable swap transaction that: "(1) [i]nvolves a swap that is listed on a [SEF or DCM]; (2) [o]ccurs away from the [SEF's or DCM's] trading system or platform and is executed pursuant to the [SEF's or DCM's] rules and procedures; (3) has a notional or principal amount at or above the appropriate minimum block size applicable to such swap ; and (4) [i]s reported subject to the rules and procedures of the [SEF or DCM] and the rules described in [part 43], including the appropriate time delay requirements set forth in § 43.5." See § 43.2, 77 FR 1,243.

[9] See proposed § 43.5, 75 FR 76174-76.

[10] Proposed § 43.5(k)(1) in the Initial Proposal provided that the time delay for the public dissemination of data for a block trade or large notional off-facility swap shall commence at the time of execution of such trade or swap. See 75 FR 76,176. Proposed § 43.5(k)(2) provided that the time delay for standardized block trades and large notional off-facility swaps (i.e., swaps that fall under CEA Section 2(a)(13)(C)(i) and (iv)) would be 15 minutes from the time of execution. Id. The Initial Proposal did not provide specific time delays for large notional off-facility swaps (i.e., swaps that fall under Section 2(a)(13)(C)(ii) and (iii)). Instead, proposed § 43.5(k)(3) provided that such swaps shall be reported subject to a time delay that may be prescribed by the Commission. Id.

The Adopting Release established time delays for the public dissemination of block trades and large notional off-facility swaps in § 43.5. See 77 FR 1247-49.

[11] See CEA Section 1a(18).

similar role or function and subject as such to foreign regulation, to transact block trades for customers who are not eligible contract participants ("non-ECPS"), if such CTA, investment adviser or foreign person has more than $25,000,000 in total AUM. The proposed rule further required that a person transacting a block trade on behalf of a customer must receive written instruction or prior consent from the customer to do so.

Furthermore, proposed § 43.5(m) of the Initial Proposal prohibited the aggregation of orders for different trading accounts in order to satisfy the minimum block size requirement, except if done on a DCM by a CTA acting in an asset managerial capacity and registered pursuant to Section 4n of the Act, or a principal thereof, including any investment adviser who satisfies the criteria of § 4.7(a)(2)(v), or a foreign person performing a similar role or function and subject as such to foreign regulation, if such CTA, investment adviser or foreign person has more than $25,000,000 in total AUM.

The Commission issued the Initial Proposal for public comment for a period of 60 days, but later reopened the comment period for an additional 45 days.[12]

1. Comments in response to the Initial Proposal

The Commission received four comment letters in response to the proposed aggregation rule. The American Benefits Council and the Committee on the Investment of Employee Benefit Assets stated that qualified investment advisers who are not CTAs should be able to aggregate block trade orders for different trading accounts.[13] Tradeweb commented that the CTAs that trade on SEFs should also be permitted to aggregate trades of behalf of their customers for

[12] The initial comment period for the Initial Proposal closed on February 7, 2011. The comment periods for most proposed rulemakings implementing the Dodd-Frank Act—including the proposed part 43 rules—subsequently were reopened for the period of April 27 through June 2, 2011.

[13] The American Benefits Council and the Committee on the Investment of Employee Benefit Assets comment letter at 3 (Feb. 7, 2011). The comment letter specifically requested that the rule be revised such that the words "including any" from the second sentence are deleted and replaced with the word "an."

purposes of block trades.[14] J.P. Morgan commented that the proposed rule appears to reflect a concern that private negotiation offers less protection to unsophisticated investors than trading through the central market, and that since all entities that transact in the OTC market already must be ECPs, the analogous concern about customer protection in the swaps market is already addressed.[15] In related comments, the Wholesale Market Brokers Association (Americas) ("WMBA") commented that "work-up" or "join-the-trade" periods be permitted and recognized to satisfy the block trade requirement.[16]

C. The Adopting Release and Further Proposal

On January 9, 2012, the Commission issued a notice of final rulemaking[17] ("Adopting Release") that finalized several provisions that were proposed in the Initial Proposal pertaining to, among other things, the reporting, public dissemination and recordkeeping requirements applicable to certain swap transactions.[18]

Based on the public comments received in response to the Initial Proposal, in the Adopting Release the Commission agreed that additional analysis was necessary prior to issuance of final rules for appropriate minimum block sizes, and accordingly determined not to make final its proposed § 43.5 rules specifying the criteria for determining block trade sizes. Instead, the Commission intended to issue a separate notice of proposed rulemaking that would

---

[14] Tradeweb comment letter at 5 (Feb. 7, 2011).

[15] J.P. Morgan comment letter at 9, n. 13 (Jan. 12, 2011).

[16] WMBA comment letter at 4-5 (Feb. 7, 2011) (commenting that "the public dissemination of incremental activity that would otherwise constitute a block trade could jeopardize identification of counterparties and materially reduce market liquidity.")

[17] Real-Time Public Reporting of Swap Transaction Data, 77 FR 1,182 (Jan. 9, 2012).

[18] Commenters are directed to the Adopting Release for a discussion of the issues addressed therein. See id.

specifically address the appropriate criteria for determining appropriate minimum block trade sizes in light of data and comments received.[19] On March 15, 2012, the Commission decided to further propose ("Further Proposal") certain other block trade provisions that were included with the Initial Proposal.[20]

After it issued the Further Proposal, the Commission determined that the aggregation provision and the provision that specified the eligible parties to a block trade, including the proposed requirement that persons transacting block trades on behalf of customers must receive prior written instruction or consent from the customer to do so, were inadvertently omitted from the Further Proposal. These provisions are the subject of this notice of proposed rulemaking.

II. Notice of Proposed Rulemaking

A. Proposed § 43.6(h)(6) - Aggregation

Proposed § 43.6(h)(6) would prohibit the aggregation of orders for different trading accounts in order to satisfy the minimum block size or cap size requirements, except that aggregation is permissible if done on a DCM or SEF by a person who: (i)(A) is a CTA registered pursuant to Section 4n of the Act or exempt from such registration under the Act, or a principal thereof, and who has discretionary trading authority or directs client accounts, (B) is an investment adviser who has discretionary trading authority or directs client accounts and satisfies the criteria of § 4.7(a)(2)(v) of this chapter, or (C) is a foreign person who performs a similar role

[19] See id. at 1,185.

[20] Commenters are directed to the Further Proposal for a discussion of the issues addressed therein. See "Procedures to Establish Appropriate Minimum Block Sizes for Large Notional Off-Facility Swaps and Block Trades," 77 FR 15,460 (Mar. 15, 2012). The comment period for the Further Proposal ended on May 14, 2012.

or function as the persons described in (A) or (B) and is subject as such to foreign regulation, and (ii) has more than $25,000,000 in total AUM.

The prohibition of aggregation of orders for different trading accounts in order to the minimum block size or cap size requirements is an integral element in ensuring the of block trading principles, and in preserving the basis for the anonymity associated with sizes. As defined in the Adopting Release, a block trade is a publicly reportable (1) involves a swap that is listed on a registered SEF or DCM; (2) occurs away from the registered SEF's or DCM's trading system or platform (and is executed pursuant to the rules of such SEF or DCM); (3) has a notional or principal amount at or above the appropriate minimum block size applicable to such swap; and (4) is reported subject to the rules and procedures of the SEF or DCM and Commission regulations, including the appropriate time delay requirements.[21] While block transactions are conducted pursuant to the rules of a SEF or DCM, by definition these transactions occur away from the SEF's or DCM's trading system or platform, where there is no pre-trade transparency. If too many trades were permitted to be aggregated and thus executable as blocks, the CEA objectives of increased transparency and price discovery for swaps trading could be undermined.[22] By prohibiting aggregation of orders for different accounts to meet the minimum block size requirement, the proposed rule would protect the principles of block trading, and would help to prevent potential circumvention of exchange-trading and of the real-time reporting obligations associated with non-block transactions. By

[21] See 77 FR 1,243.

[22] J.P. Morgan Comment letter at 5 (Jan. 12, 2011).

presumption, the aggregation of orders for different accounts to meet the minimum block size threshold would be prohibited.

Indeed, in the futures market, all block trade rules approved by the Commission have have included an aggregation prohibition (with the discrete exception of block trades done done through certain CTAs). Accordingly, in the futures market, where market participants have engaged in block transactions for years, DCMs that permit block trading have rules that prohibit the aggregation of orders for different trading accounts to meet the minimum block size requirement.[23]

As proposed in this release, the rule also would prohibit aggregation in order to meet the cap size requirements. A cap size is defined in the Further Proposal as the maximum notional or principal amount of a publicly reportable swap transaction that is publicly disseminated.[24] A transaction that meets the cap size requirement would be eligible to mask the total size of the transaction if it equals or exceeds the cap size for a given swap category.[25] The Commission adopted cap sizes in order to help to protect the anonymity of counterparties' market positions and business transactions, and to mitigate the potential impact that real-time public reporting of extraordinarily large positions could have in reducing market liquidity.[26] By preventing

---

[23] The following DCMs have rules permitting block trading: Cantor Futures Exchange, L.P. (rule IV-16); CBOE Futures Exchange LLC (rule 415); Chicago Board of Trade (rule 526); CME (rule 526); ELX Futures, L.P. (rule IV-16); Eris Exchange, LLC (rule 601); Green Exchange, LLC (rule 602); ICE Futures (rule 4.31); Nasdaq OMX Futures Exchange, Inc. (rule E23); New York Mercantile Exchange, Inc. (rule 526); NYSE Liffe US, LLC (rule 423); and OneChicago LLC Futures Exchange (rule 417). Each of the aforementioned DCMs also have rules prohibiting aggregation of orders to meet minimum block transaction size: Cantor Futures Exchange, L.P. (rule IV-16(K)); CBOE Futures Exchange LLC (rule 415(a)(i)); Chicago Board of Trade (rule 526A); CME (rule 526A); ELX Futures, L.P. (rule IV-16(a)); Eris Exchange, LLC (rule 601(b)(1)); Green Exchange, LLC (rule 602(a)); ICE Futures (rule 4.31(a)(ii)(B)); Nasdaq OMX Futures Exchange, Inc. (rule E23(d)); New York Mercantile Exchange, Inc. (rule 526A); NYSE Liffe US, LLC (rule 423(a)(1)); and OneChicago LLC Futures Exchange (rule 418(a)(i)).

[24] 77 FR 15, 516.

[25] 77 FR 15,489-90.

[26] Id.

aggregation of orders to meet the cap size requirement, the proposed rule will help to ensure that cap sizes are used for the specific purpose for which they are intended (extraordinarily large positions), and will help to prevent potential circumvention of the real-time reporting obligations.

The proposed rule further provides that aggregation of orders for different trading accounts for purposes of the block size or cap size requirements may be permitted on a DCM or SEF if done by a person who: (i)(A) is a CTA who is registered pursuant to Section 4n of the Act or is exempt from registration under the Act, or a principal thereof, and has discretionary trading authority or directs client accounts, (B) is an investment adviser who has discretionary trading authority or directs client accounts and satisfies the criteria of § 4.7(a)(2)(v) of the Commission's regulations, or (C) is a foreign person who performs a similar role or function to the persons described in (A) or (B) and is subject as such to foreign regulation, and (ii) has more than $25,000,000 in total AUM. As noted above, DCMs that permit block trading in connection with futures contracts currently prohibit aggregation of orders to meet the block size requirement, and a majority of these DCMs have substantially similar rules that allow aggregation in such context if done by certain CTAs, investment advisers and foreign persons.[27]

The Commission is seeking comments on whether this exception to the prohibition of aggregation of orders is appropriate in the context of the swaps market. The Commission seeks comments on whether such an exception should be available to other categories of Commission

[27] A majority of DCMs currently maintain similar rules permitting certain CTAs, investment advisors and foreign persons to aggregate. See, e.g., CME Rulebook, rule 526 (providing an exception for block transactions by permitting aggregation if done by a CTA registered or exempt from registration under the Act, including without limitation, any investment adviser registered or exempt from registration under the Investment Adviser's Act of 1940 . . . provided that such advisers have total AUM exceeding $25 million and the block trade is suitable for the customers of such advisors. See also, CBOE Futures Exchange LLC (rule 415(a(i)); Chicago Board of Trade (rule 526I); CME (rule 526I); ELX Futures, L.P. (rule IV-16(a)); Eris Exchange, LLC (rule 601(b)(10)); Green Exchange, LLC (rule 602(j)); ICE Futures ((rule 4.31(a)(ii)(B)); Nasdaq OMX Futures Exchange, Inc., (rule E23); New York Mercantile Exchange, Inc. (rule 526I); NYSE Liffe US, LLC (rule 423(a)(i)); and OneChicago LLC Futures Exchange (rule 417(a)(i)).

registrants, and if so, why? Additionally, the Commission seeks comments on whether the $25 million AUM requirement for the specified account controllers is appropriate in the context of block transactions for swaps? Further, the Commission seeks comments on whether the $25 million AUM requirement should include only swaps assets, or be based per asset class, or be different for the five asset classes of swaps? In addition to these specific questions, the Commission requests comments on all aspects of this notice of proposed rulemaking.

B. Proposed § 43.6(i) – Eligible block trade parties

The Commission is also proposing under new § 43.6(i)(1) a provision that describes the eligible parties to a block trade. The proposed provision provides that parties to a block trade must be "eligible contract participants," as that term is defined under Section 1a(18) of the CEA and the Commission's regulations. The proposed rule includes an exception to the ECP requirement by providing that a DCM may allow: (i) a CTA registered pursuant to Section 4n of the Act, or exempt from registration under the Act, or a principal thereof, who has discretionary trading authority or directs client accounts, (ii) an investment adviser who has discretionary trading authority or directs client accounts and satisfies the criteria of § 4.7(a)(2)(v) of the Commission's regulations, or (iii) a foreign person who performs a similar role or function to the persons described in (i) or (ii) and is subject as such to foreign regulation, to transact block trades for customers who are not ECPs, if such CTA, investment adviser or foreign person has more than $25,000,000 in total AUM.[28]

In the current futures market, all DCMs require that parties to block trades must be ECPs. A majority of these DCMs permit certain CTAs, investment advisers and foreign persons to

[28] Parties that are non-ECPs may not enter into any swap transactions, including blocks, except on or subject to the rules of a DCM. Specifically, section 2(e) of the CEA provides that "[i]t shall be unlawful for any person, other than an eligible contract participant, to enter into a swap unless the swap is entered into on, or subject to the rules of, a board of trade designated as a contract market under section 5." 7 USC 2(e).

transact a block trade on behalf of their non-ECP customers. The proposed rule, including the limited exception, is currently reflected in the rulebooks of numerous DCMs that permit block trading in the futures market.[29]

Proposed § 43.6(i)(2) further provides that a person transacting a block trade on behalf of a customer must receive prior written instruction or consent from the customer to do so. Such instruction or consent may be provided in a power of attorney or similar document by which the customer provides the person with discretionary trading authority or the authority to direct the trading in its account. This rule also is substantially similar to the block trading rules maintained by existing DCMs.

III. Related Matters

A. Regulatory Flexibility Act

The Regulatory Flexibility Act (''RFA'') requires that agencies consider whether the rules they propose will have a significant economic impact on a substantial number of small entities and, if so, provide a regulatory flexibility analysis respecting the impact.[30] The RFA focuses on direct impact to small businesses and not on indirect impacts on these businesses, which may be tenuous and difficult to discern.[31] The CFTC believes that this proposal would not have a significant economic impact on a substantial number of small entities.

1. Effect of the Proposed Rulemaking

[29] Most DCMs that permit block trading require that parties to the block trade must be ECPs with a limited exception for CTAs. The following DCMs have rules excepting CTAs from the requirement that parties to a block trade must be ECPs: CBOE Futures Exchange LLC (rule 415(a)(ii)); Chicago Board of Trade (rule 526I); CME (rule 526I); ELX Futures, L.P. (rule IV-16(c)); Eris Exchange, LLC (rule 601(b)(10)); Green Exchange, LLC (rule 602(a) and (j)); ICE Futures ((rule 4.31(a)(i)); Nasdaq OMX Futures Exchange, Inc., (rule E23(d)); New York Mercantile Exchange, Inc. (rule 526I); NYSE Liffe US, LLC (rule 423(a)(ii)); and OneChicago LLC Futures Exchange (rule 417(a)(ii)).

[30] See 5 U.S.C. 601 et seq.

[31] See Whitman v. Am. Trucking Ass'ns, 531 U.S. 457 (2001); Am. Trucking Assns. v. EPA, 175 F.3d 1027, 1043 (D.C. Cir. 1985); Mid-Tex Elec. Coop., Inc. v. FERC, 773 F.2d 327, 340 (D.C. Cir. 1985).

This release proposes a rule that would prohibit the aggregation of orders for different trading accounts in order to satisfy the minimum block size, or cap size requirement. The proposed rule further provides that aggregation is permissible if done on a DCM or SEF by a person who: (i)(A) is a CTA who is registered pursuant to Section 4n of the Act, or is exempt from registration under the Act, or a principal thereof, and has discretionary trading authority or directs client accounts, (B) is an investment adviser who has discretionary trading authority or directs client accounts and satisfies the criteria of § 4.7(a)(2)(v) of the Commission's regulations, or (C) is a foreign person who performs a similar role or function to the persons described in (A) or (B) and is subject as such to foreign regulation, and (ii) has more than $ 25,000,000 in total AUM.

This release also proposes under new § 43.6(i)(1) a provision that describes the eligible parties to a block trade. The proposed rule provides that parties to a block trade must be "eligible contract participants," as that term is defined under Section 1a(18) of the CEA and the Commission's regulations. The proposed rule further provides that a DCM may allow: (i) a CTA who is registered pursuant to Section 4n of the Act, or exempt from registration under the Act, or a principal thereof, who has discretionary trading authority or directs client accounts, (ii) an investment adviser who has discretionary trading authority or directs client accounts and satisfies the criteria of § 4.7(a)(2)(v) of the Commission's regulations, or (iii) a foreign person who performs a similar role or function to the persons described in (i) or (ii) and is subject as such to foreign regulation, to transact block trades on behalf of their customers who are not eligible contract participants, if such CTA, investment adviser or foreign person has more than $25,000,000 in total AUM.

The CFTC is of the view that this proposal may affect primarily the following entities: DCMs, futures commission merchants ("FCMs"), ECPs, swap dealers, major swap participants, certain CTAs, SEFs and certain investment advisers. The majority of entities impacted by this proposed rulemaking have been determined by the Commission not to be small entities. To the extent that a small number of small entities may be affected by the proposed rules, the Commission believes, as described below, that the proposed rules would not have a significant economic impact on a substantial number of such entities.

2. Specific Entities That May Be Small Entities

As noted above, the Commission has previously determined that DCMs, FCMs, and ECPs are not small entities for purposes of the Regulatory Flexibility Act.[32] Certain other entities that may be affected by this rulemaking, including SDs, MSPs and SEFs, have been certified by the Commission not to be small entities in other recent rulemakings implementing the requirements of the Dodd-Frank Act.[33]

a. Entities affected under § 43.6(h)(6): FCMs, CTAs and investment advisers.

As noted above, the CFTC previously has determined that registered FCMs are not small entities for purposes of the RFA based upon, among other things, the registration requirements that FCMs must meet, including certain minimum financial requirements that enhance the protection of customers' segregated funds and protect the financial condition of FCMs

[32] See, respectively and as indicated, 47 FR 18618, 18619, Apr. 30, 1982 (DCMs, CPOs, FCMs, and large traders); and, 66 FR 20740, 20743, Apr. 25, 2001 (ECPs).

[33] See respectively, Registration of Swap Dealers and Major Swap Participants, 77 FR 2613, 2620 (Jan. 19, 2012) (swap dealers and major swap participants); Requirements for Derivatives Clearing Organizations, Designated Contract Markets, and Swap Execution Facilities Regarding the Mitigation of Conflicts of Interest, 75 FR 63732, 63746 (Oct. 18, 2010) (SEFs); Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping, 76 FR 29818, 29868 (May 23, 2011) (Products).

generally.[34] With respect to certain CTAs[35] and investment advisers who would not be permitted to aggregate under the proposed rule, the Commission notes that the same provisions embodied in the proposed rule are currently required by DCM rules (under rules accepted by the Commission) and thus, such entities currently must comply with the same aggregation prohibition. Thus, all DCMs that permit aggregation for purposes of the block size requirement, only permit aggregation by CTAs, investment advisers and foreign persons that have more than $25,000,000 in total AUM. Accordingly, the Commission believes that this rule does not impact entities that heretofore have not been able to aggregate. To the extent that certain CTAs and investment advisers with less than $25,000,000 AUM are not currently permitted to aggregate, the Commission's codification of these rules would not have any significant economic impact on a substantial number of small entities.

b. Entities affected under § 43.6(i)(1): Certain non-ECP participants on DCMs, certain investment advisors and FCMs.

New § 43.6(i)(1) provides that parties to a block trade must be "eligible contract participants,"[36] as that term is defined under Section 1a(18) of the CEA and § 1.3 of the Commission's regulations, except for certain CTAs, investment advisers or foreign persons performing a similar role or function having more than $25,000,000 in total AUM, which may transact block trades for customers who are not ECPs. As indicated above, certain CTAs and investment advisers that have less than $25,000,000 in AUM would not be covered under the proposed rule because the provision embodied in the proposed rule is substantially the same as is currently required by DCM rules (under rules accepted by the Commission). Similarly, any non-

[34] See supra note 32.

[35] The Commission may determine on a case-by-case basis whether CTAs are not small entities for the purpose of the RFA based upon a case by case determination. See 47 FR 18618, 18620(Apr. 30, 1982).

[36] ECPs have been determined not to be small entities. See 66 FR 20740, 20743(Apr. 25, 2001).

ECP participants who trade on DCMs also would be prohibited under current DCM rules from directly entering into a block transaction unless their qualifying CTA, investment adviser, or foreign person acts on their behalf. To the extent that these entities are not currently permitted to aggregate, the Commission's codification of these rules would not have any significant economic impact on a substantial number of small entities. Accordingly, the Chairman, on behalf of the Commission, hereby certifies pursuant to 5 U.S.C. 605(b) that the proposed rules will not have a significant economic impact on a substantial number of small businesses. Nonetheless, the Commission specifically requests comment on the economic impact that this notice of proposed rulemaking may have on small entities.

B. Paperwork Reduction Act

The purposes of the Paperwork Reduction Act of 1995, 44 U.S.C. 3501 et seq. ("PRA") are, among other things, to minimize the paperwork burden to the private sector, ensure that any collection of information by a government agency is put to the greatest possible uses, and minimize duplicative information collections across the government.[37] The PRA applies to all information, "regardless of form or format," that a government is "obtaining, causing to be obtained, [or] soliciting" and requires "disclosure to third parties or the public, of facts or opinions," when the information collection calls for "answers to identical reporting or recordkeeping requirements imposed, on ten or more persons[.]"[38] The PRA requirements have been determined to include not only mandatory but also voluntary information collections, and include both written and oral communications.[39]

---

[37] See 44 U.S.C. 3501.

[38] 44 U.S.C. 3502.3(A)(i).

[39] See 5 CFR 1320.3(c)(1).

The proposed rules would not impose any new recordkeeping or information collection requirements, or other collections of information that require approval of the Office of Management and Budget ("OMB") under the PRA. The proposed rules are covered by existing collection requirements and would not change existing collection requirements.[40] The Commission invites public comment on the accuracy of its estimate that no additional recordkeeping or information collection requirements or changes to existing collection requirements would result from the rules proposed herein.

C. Cost-Benefit Considerations

Section 15(a) of the CEA[41] requires the Commission to consider the costs and benefits of its actions before promulgating a regulation or issuing an order under the CEA. Section 15(a) further specifies that the costs and benefits shall be evaluated in light of the following five broad areas of market and public concern: (1) protection of market participants and the public; (2) efficiency, competitiveness, and financial integrity of futures markets; (3) price discovery; (4) sound risk management practices; and (5) other public interest considerations. The Commission considers the costs and benefits resulting from its discretionary determinations with respect to the Section 15(a) factors.

The baseline for the Commission's assessment of costs and benefits attributable to its discretionary actions in this rulemaking is the costs and benefits that would otherwise exist today (i.e., post-Dodd-Frank Act enactment) absent this Commission action. The Commission recognizes that before the Dodd-Frank Act, swap transactions were executed over-the-counter and were not publicly reported. One of the implications of the Dodd-Frank Act is that most swap

[40] See 77 FR 1182 (Jan. 9, 2012), as amended by the Further Proposal. OMB has assigned control number 3038–0070 to the existing collection of information, which is titled "Part 43—Real-Time Public Reporting,"

[41] 7 U.S.C. 19(a).

transactions are required to be publicly disseminated by SDRs as soon as technologically practicable, unless the notional value of the swap transaction meets the minimum block trade threshold.[42] That is the baseline for the Commission's proposed assessment of costs and benefits in this release. The Commission proposes that costs and benefits with respect to block trade thresholds are already accounted for in the Further Proposal and that this rule only considers the additional costs and benefits relevant to proposed § 43.6(h)(6) and proposed § 43.6(i).

1. Costs and Benefits Relevant to Proposed § 43.6(h)(6) - Aggregation

The Commission is proposing § 43.6(h)(6) to specify that, except as otherwise provided, it is impermissible to aggregate orders for different accounts in order to satisfy minimum block trade or cap size requirements. The proposed rule further provides that aggregation may be permitted on a DCM or SEF if done by a person who: (i)(A) is a CTA who is registered pursuant to Section 4n of the Act or is exempt from registration under the Act, or a principal thereof, and has discretionary trading authority or directs client accounts, (B) is an investment adviser who has discretionary trading authority or directs client accounts and satisfies the criteria of § 4.7(a)(2)(v) of the Commission's regulations, or (C) is a foreign person who performs a role or function similar to the persons described in (A) or (B) and is subject as such to foreign regulation, and (ii) has more than $25,000,000 in total AUM.

Costs

The Commission expects that there will be some incremental cost attendant to compliance with proposed § 43.6(h)(6), and seeks data from the public in order to quantify the same. The Commission believes that the overall benefits to the market of allowing for the

[42] The Commission notes that for an initial interim period, as outlined in § 43.5 of the Adopting Release, all transactions will be treated as block trades and will enjoy delayed reporting temporarily.

aggregation of orders under certain circumstances (i.e., if done on a designated contract market or a swap execution facility by certain CTAs, investment advisers or foreign persons) will mitigate costs of reduced market liquidity that could result from execution of such transactions away from the centralized marketplace. The Commission also expects there to be some advisors who will be prohibited from aggregating orders for different trading accounts in order to satisfy the minimum block size, or cap size requirements. The Commission also proposes that as a result of some advisors not being allowed to aggregate, there might be some minimal unquantifiable cost associated with a decrease in competition among such traders in the market. The Commission seeks comment on these and any other costs that may result from this proposal. In particular, and as noted above, the WMBA claimed in its comment letter that "work-up" or "join-the-trade" periods be permitted to satisfy the block trade requirements, and that "the public dissemination of incremental activity that would otherwise constitute a block trade could jeopardize identification of counterparties and materially reduce market liquidity."[43] The Commission seeks comment on the costs and benefits of the rules proposed in this release with respect to the specific implications claimed by WMBA.

Benefits

The proposed rule is designed, in large part, to prevent circumvention of the exchange trading requirements and of the real-time reporting obligations associated with non-block transactions. Absent this prohibition, the goals of the Commission's regulations regarding block trading, namely increased transaction transparency, better price discovery and improved competitiveness in the markets as well as better risk management, could be frustrated by those whose trades individually fail to meet the minimum block trade threshold (and cap size threshold

[43] WMBA comment letter at 4-5 (Feb. 7, 2011).

as a result), but nevertheless achieve the benefits intended for extraordinarily large positions by aggregating those individual trades. In other words, such entities would be able to evade the exchange-trading and reporting obligations that are integral to price transparency. The Commission seeks comment on these and any other benefits that may result from this proposal.

Section 15(a) Factors

(1) Protection of market participants and the public.

The Commission believes that the proposed rule would protect market participants from unfair practices by preventing trades that do not meet the minimum block trade threshold from enjoying extended reporting times. This requirement would mean that trades that are not extraordinarily large, and hence, that do not need extra reporting time would not qualify as block trades and would be made public as soon as technologically practicable. Hence, the proposed rule would increase transparency of non-block transactions, and thus, would protect market participants by informing their trading determinations through increased transparency and price discovery.

(2) Efficiency, competitiveness, and financial integrity of the futures markets.

The Commission expects the prohibition of aggregation of trades to improve efficiency and competitiveness in the markets by allowing more trades to be reported without the time delay that is applied to qualifying block trades. This requirement would mean that a higher number of trades would be eligible for real time reporting, and that would increase market transparency as well as promote competition in the swap markets. The rule also would protect the integrity of the derivatives market by ensuring that smaller trades, which do not qualify as block transactions, are executed on the trading system where there is pre-trade and post-trade transparency.

The Commission also recognizes that advisors who are prohibited from aggregating orders in order to satisfy the minimum block size or cap size requirements might not trade at the most favorable prices in the market, which might have a negative effect on the number of such traders in the market. While the Commission expects that competition in the market may be negatively affected as a result of prohibiting aggregation, the Commission anticipates that the positive effects of the proposed rule on competition outweigh its negative effects.

(3) Price discovery.

The Commission expects the proposed rule to improve price discovery in the swap markets by preventing aggregation of trades and as a result promoting more trades to be publicly reported as soon as technologically practicable. This would result in enhanced swap market price discovery, since market participants and the public would be able to observe real-time pricing information for a higher percentage of transactions in the market. In addition, the Commission expects that the rule would enhance price discovery by ensuring that smaller trades, which do not qualify as block transactions, are executed on the trading system where there is pre-trade and post-trade transparency and where buyers and sellers may make informed trading decisions based on the market's transparency.

(4) Sound risk management practices.

The Commission anticipates that the proposed criteria, if adopted, would likely result in enhanced price discovery as discussed above. With better and more accurate data, swap market participants would likely be better able to measure and manage risk. The Commission proposes that if the prohibition of aggregation of trades was not adopted, swap transactions may not be reported to an SDR "as soon as technologically practicable." The Commission also proposes that by preventing this delay in the reporting period of a swap transaction to an SDR, the

Commission will possess the information it needs to monitor the transfer and positions of risk among counterparties in the swaps market.

(5) Other public interest considerations.

The Commission has not identified any other public interest considerations regarding the proposed rule.

2. Costs and Benefits Relevant to Proposed § 43.6(i) – Eligible Block Trade Parties

Costs

Proposed § 43.6(i)(1) requires that parties to a block trade must be eligible contract participants, as defined under the CEA and Commission regulations, except that a DCM may allow: (i) a CTA registered pursuant to Section 4n of the Act or exempt from registration under the Act, or a principal thereof, and who has discretionary trading authority or directs client accounts, (ii) an investment adviser who has discretionary trading authority or directs client accounts and satisfies the criteria of § 4.7(a)(2)(v) of the Commission's regulations, or (iii) a foreign person who performs a similar role or function to the persons described in (i) or (ii) and is subject as such to foreign regulation, to transact block trades for customers who are not eligible contract participants, if such CTA, investment adviser or foreign person has more than $25,000,000 in total AUM. This proposed rule codifies, in part, the requirement under Section 2(e) of the CEA, which requires that "[i]t shall be unlawful for any person, other than an eligible contract participant, to enter into a swap unless the swap is entered into on, or subject to the rules of....a designated contract market." In addition, the provisions allowing certain entities (as described in this release) to enter into block trades on behalf of their non-ECP customers on DCMs is substantially similar to the existing DCM rules that allow block trading in the futures market.

Proposed § 43.6(i)(2) further provides that no person may conduct a block trade on behalf of a customer unless the person receives prior written instruction or consent to do so. The proposed rule further provides that such instruction or consent may be provided in the power of attorney or similar document by which the customer provides the person with discretionary trading authority or the authority to direct the trading in its account. The Commission is of the view that the cost associated with the written instruction or consent is minimal. The Commission estimates that a prior written instruction or consent requirement would impose an initial non-recurring burden of approximately 2 personnel hours at an approximate cost of $155.54 for each CTA, investment adviser or foreign person.[44]

Benefits

The Commission has determined that the benefits of proposed § 43.6(i) are significant. The proposed rule, if adopted, would allow customers who are not ECPs to engage in block trade transactions through certain entities as outlined in the rule. By permitting certain CTAs, investment advisers and foreign persons to transact swaps on behalf of non-ECP customers, the

[44] Using wage rate estimates based on salary information for the securities industry compiled by the Securities Industry and Financial Markets Association ("SIFMA"), the estimate is calculated as follows: Compliance manager at 2 hours. A senior programmer's adjusted hourly wage is $77.77, estimated using the following calculations:

(1) [(2009 salary + bonus) * (salary growth per professional type, 2009-2010)] = Estimated 2010 total annual compensation. The most recent data provided by the SIFMA report describe the 2009 total compensation (salary + bonus) by professional type, the growth in base salary from 2009 to 2010 for each professional type, and the 2010 base salary for each professional type; thus, the Commission estimated the 2010 total compensation for each professional type, but, in the absence of similarly granular data on salary growth or compensation from 2010 to 2011 and beyond, did not estimate dollar costs beyond 2010.

(2) [(Estimated 2010 total annual compensation) / (1,800 annual work hours)] = Hourly wage per professional type.]

(3) [(Hourly wage) * (Adjustment factor for overhead and other benefits, which the Commission has estimated to be 1.3)] = Adjusted hourly wage per professional type.]

(4) [(Adjusted hourly wage) * (Estimated hour burden for compliance)] = Dollar cost of compliance for each hour burden estimate per professional type.]

rule provides important safeguards for non-ECPs when entering into block transactions in swaps. The Commission believes that access to block trades would allow customers who are not ECPs to diversify their risk or improve their investment strategies. In addition, the Commission also anticipates the access to block trades for non-ECPs to increase their participation in swap markets, increasing liquidity in the markets for everyone.

Section 15(a) Factors

(1) Protection of market participants and the public.

The Commission does not anticipate the proposed rule to have any significant effect on the protection of market participants and the public.

(2) Efficiency, competitiveness, and financial integrity of the futures markets.

The Commission expects the proposed rule to improve competitiveness in the markets by allowing customers who are not ECPs to have access to block trades through certain CTAs, investment advisers and foreign persons. The Commission anticipates an increase in competitiveness due to the fact that more customers would use the swap markets as a result of this rule. An increased participation in a market would also serve to increase liquidity, as well as competition, in that market.

(3) Price Discovery.

The Commission does not anticipate the proposed rule to have any significant effect on price discovery in the market.

(4) Sound risk management practices.

The Commission does not anticipate the proposed rule to have any significant effect on risk management practices.

(5) Other public interest considerations.

The Commission has not identified any other public interest considerations regarding the proposed rule.

The Commission requests comments on its cost and benefit considerations with respect to the proposed rule, and any alternatives. The Commission specifically requests that commenters provide data from which the Commission may quantify the costs or benefits of the proposed rule.

IV. Rule Text

List of Subjects in 17 CFR Part 43

Large notional off-facility trades, block trades, appropriate minimum block sizes, real-time public reporting, public dissemination, cap size, anonymity, swap category

1. The authority citation for part 43 shall continue to read as follows:

Authority: 7 U.S.C. 2(a), 12a(5) and 24a, amended by Pub. L. 111-203, 124 Stat. 1376 (2010).

2. Add section 43.6(h)(6) to part 43 to read as follows:

§ 43.6(h)(6) Aggregation.

Except as otherwise stated in this paragraph, the aggregation of orders for different accounts in order to satisfy the minimum block trade size or the cap size requirement is prohibited. Aggregation is permissible on a designated contract market or swap execution facility if done by a person who:

(i) (A) is a commodity trading advisor registered pursuant to Section 4n of the Act, or exempt from registration under the Act, or a principal thereof, who has discretionary trading authority or directs client accounts,

(B) is an investment adviser who has discretionary trading authority or directs client accounts and satisfies the criteria of § 4.7(a)(2)(v) of this chapter, or

(C) is a foreign person who performs a similar role or function as the persons described in subparagraphs (A) or (B) and is subject as such to foreign regulation; and,

(ii) has more than $25,000,000 in total assets under management.

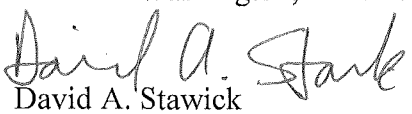
3. Add Section 43.6(i) to part 43 to read as follows:

§ 43.6(i) Eligible Block Trade Parties.

(1) Parties to a block trade must be "eligible contract participants," as defined in Section 1a(18) of the Act and the Commission's regulations. However, a designated contract market may allow: (i) a commodity trading advisor registered pursuant to Section 4n of the Act, or exempt from registration under the Act, or a principal thereof, who has discretionary trading authority or directs client accounts, (ii) an investment adviser who has discretionary trading authority or directs client accounts and satisfies the criteria of § 4.7(a)(2)(v) of this chapter, or (iii) a foreign person who performs a similar role or function as the persons described in (i) or (ii) of this paragraph and is subject as such to foreign regulation, to transact block trades for customers who are not eligible contract participants if such commodity trading advisor, investment adviser or foreign person has more than $25,000,000 in total assets under management.

(2) A person transacting a block trade on behalf of a customer must receive prior written instruction or consent from the customer to do so. Such instruction or consent may be provided in the power of attorney or similar document by which the customer provides the person with discretionary trading authority or the authority to direct the trading in its account.

Issued in Washington, DC on June 20, 2012, by the Commission.



David A. Stawick
Secretary of the Commission

Appendix to Rules Prohibiting the Aggregation of Orders to Satisfy Minimum Block Sizes or Cap Size Requirements, and Establishing Eligibility Requirements for Parties to Block Trades

Commission Voting Summary

NOTE: The following appendix will not appear in the Code of Federal Regulations

On this matter, Chairman Gensler and Commissioners Sommers, Chilton, O'Malia and Wetjen voted in the affirmative; no Commissioner voted in the negative.