



## U.S. COMMODITY FUTURES TRADING COMMISSION

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### Division of Market Oversight

CFTC Letter No. 15-60  
No-Action  
November 2, 2015  
Division of Market Oversight

#### **Re: Extension of No-Action Relief for Swap Execution Facilities from Certain “Block Trade” Requirements in Commission Regulation 43.2**

Ladies and Gentlemen:

On September 19, 2014, the Division of Market Oversight (“Division”) of the Commodity Futures Trading Commission (the “Commission” or “CFTC”) issued CFTC Letter 14-118 (“No Action Letter 14-118”) to provide relief for swap execution facilities (“SEFs”) from the requirement in §43.2 that a swap block trade must “[o]ccur[ ] away from the registered [SEF’s] or [DCM’s] trading system or platform.”<sup>1</sup> The no-action letter provided that the Division would not recommend enforcement action against a SEF which has rules and/or procedures that provide for the use of a SEF trading system or platform to facilitate the execution of block trades for swaps that are intended to be cleared,<sup>2</sup> and thus not complying with the requirement that a swap block trade occur away from the trading system or platform under §43.2, provided that certain conditions set forth in the letter are met. Absent further action from the Division, No-Action Letter 14-118 will expire on December 15, 2015. By letter dated September 30, 2015, the Wholesale Markets Brokers’ Association, Americas (“WMBAA”) requested that the relief granted in No-Action Letter 14-118 be extended until November 15, 2016 (“WMBAA Letter”).

#### **Background**

Commission Regulation 43.2 defines a “block trade” as, among other things, a publicly reportable swap transaction that “[o]ccurs away from the registered [SEF’s] or [DCM’s] trading system or platform and is executed pursuant to the registered [SEF’s] or [DCM’s] rules and procedures” (hereinafter the “occurs away” requirement). In a subsequent rulemaking establishing appropriate minimum sizes for block trades, the Commission further clarified this language by stating that “[by] definition, a block trade must occur away from the SEF[’s] trading system or platform” and that “[a]ny swap that is executed on a SEF[’s] or DCM’s trading system or

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<sup>1</sup> See CFTC Letter 14-118.

<sup>2</sup> Swaps that are intended to be cleared are swaps that are (i) of a type accepted for clearing by a DCO, and (ii) intended to be submitted for clearing contemporaneously with execution.

platform, regardless of whether it is for a size at or above the appropriate minimum block size for such swap, is not a block trade under this definition....”<sup>3</sup>

Commission regulation 1.73 requires a Futures Commission Merchant (“FCM”) that is a clearing member (“Clearing FCM”) of a registered derivatives clearing organization (“DCO”) to establish risk-based limits and to screen orders for compliance with those limits. Staff guidance specifies that this requirement applies to orders for execution on or subject to the rules of a SEF or DCM, regardless of the method of execution.<sup>4</sup> Commission regulation 37.702(b) requires a SEF to coordinate with each DCO to which it submits transactions for clearing and have rules and procedures to facilitate prompt and efficient processing by DCOs in accordance with Commission regulation 39.12(b)(7).<sup>5</sup> Staff guidance specifies that a SEF must facilitate pre-execution screening by each Clearing FCM on an order-by-order basis.<sup>6</sup>

### **Relief Requested**

In its letter, WMBAA states, among other things, that “SEFs are uniquely positioned to ensure that FCMs have timely, accurate information needed to facilitate pre-execution credit checks.”<sup>7</sup> WMBAA’s letter also asserts, among other things, that Commission regulations should “be amended to provide market participants with a permanent solution.”<sup>8</sup> However, as an interim measure, WMBAA believes that “an extension of the relief granted under No-Action Letter 14-118 would allow the WMBAA member firms, other SEFs, market participants and the Commission time to consider and develop best practices and a permanent solution to the issues attendant to block trades, including amendments to the Commission’s regulations.”<sup>9</sup> Therefore, WMBAA requests an extension of the no-action relief in No-Action Letter 14-118 be provided by the Division until November 15, 2016.<sup>10</sup>

### **No-Action Relief**

The Division agrees that SEFs can facilitate the pre-trade credit checks that are required for FCMs and SEFs to comply with §§1.73 and 37.702(b), respectively.<sup>11</sup> Therefore, the Division has

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<sup>3</sup> See Procedures To Establish Appropriate Minimum Block Sizes for Large Notional Off-Facility Swaps and Block Trades, 78 Fed. Reg. 32866, 32904 n.425 (May 31, 2013).

<sup>4</sup> See Staff Guidance on Swaps Straight-Through Processing (Sept. 26, 2013) (“STP Guidance”)

<sup>5</sup> Commission regulation 39.12(b)(7) requires DCOs to accept or reject all trades executed competitively on a SEF or DCM as quickly as would be technologically practicable as if fully automated systems were used.

<sup>6</sup> See STP Guidance.

<sup>7</sup> WMBAA further states in support of its request for relief that execution of block trades on SEFs would further the goal of promoting swaps trading on SEFs and would “promote[] transparency and regulatory oversight as such trades would be required to comport with the core principles and other requirements for SEFs.” See WMBAA Letter at 2.

<sup>8</sup> Id.

<sup>9</sup> Id.

<sup>10</sup> Id.

<sup>11</sup> As stated in No Action Letter 14-118, the Division understood that an FCM that has no involvement in a block transaction occurring away from a SEF’s trading system or platform would be unable to implement a credit screening of the trade prior to the counterparties’ execution of the block. See CFTC Letter 14-118 at 2-

determined to extend the no-action relief provided in No-Action Letter 14-118. During the extended period of relief, Division staff will continue to review and evaluate SEF trading practices and functionalities for pre-execution credit checks and will consider, develop and evaluate best practices and more permanent solutions to the issues involved in screening block trade orders for compliance with risk-based limits including, if appropriate, amendments to Commission regulations. The Division will not recommend that the Commission take enforcement action against any SEF which has rules and/or procedures that provide for the use of a SEF trading system or platform to facilitate the execution of block trades for swaps that are intended to be cleared and thus not complying with the “occurs away” requirement under §43.2 during the extended period of relief, provided that the conditions set forth in No-Action Letter 14-118 continue to be met. These conditions are as follows:

- The block trade is not executed on the SEF’s Order Book functionality, as defined in §37.3(a)(3);<sup>12</sup>

- The SEF adopts rules pertaining to cleared blocks that indicate that the SEF is relying on the relief provided in this no-action letter<sup>13</sup> and require each cleared block trade execution on a non-Order Book trading system or platform to comply with the requirements set forth in the block trade definition in §43.2. Specifically, the block trade must:

1. Involve a swap that is listed on a registered SEF;
2. Be executed pursuant to the SEF’s rules and procedures;
3. Meet the notional or principal amount at or above the appropriate minimum block size applicable to the swap; and
4. Be reported to a swap data repository pursuant to the SEF’s rules and procedures and the Commission’s rules and regulations.

- The FCM completes the pre-execution credit check pursuant to §1.73 at the time the order for a block trade enters the SEF’s non-Order Book trading system or platform;<sup>14</sup> and

- The block trade is subject to void ab initio requirements where the swap is rejected on the basis of credit.<sup>15</sup>

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3. The Division confirms that this no action, similar to No Action Letter 14-118 does not affect the compliance requirements for pre-trade credit checks and, as such, does not extend relief from the obligation to obtain a pre-trade credit for block transactions which occur away from the trading system or platform.

<sup>12</sup> The Division notes that while block trades may not be facilitated through a SEF’s Order Book functionality, pursuant to this no-action letter, SEFs are permitted to use RFQ functionalities to facilitate the execution of a block trade. Also, the Division notes that a block trade executed through a SEF’s RFQ functionality pursuant to this no-action relief would not be subject to the minimum participant requirement set forth in § 37.9(a)(3). Finally, the Division notes that trades above the minimum block size may occur on the SEF’s Order Book, however, they will not receive treatment as block trades and will not be afforded a reporting time delay.

<sup>13</sup> These rules should include a citation to this no-action letter as “NAL 15- 60, expiring November 15, 2016.”

<sup>14</sup> Consistent with the STP Guidance, the §1.73 credit check must be done before execution, no matter the means of execution.

The relief shall expire at 11:59 pm, Eastern Standard Time, on November 15, 2016.

### Conclusion

Market participants should be aware that the no-action position taken herein does not excuse affected persons from compliance with any other applicable requirements of the Commodity Exchange Act or the Commission's regulations thereunder, in particular, the applicable swap data reporting requirements, clearing requirements, pre-execution credit check requirements, and straight-through processing requirements.<sup>16</sup> This letter, and the no-action position taken herein, represent the views of the Division only, and do not represent the position or views of the Commission or of any other division or office of the Commission's staff. As with all no-action letters, the Division retains the authority to condition further, modify, suspend, terminate or otherwise restrict the terms of the no-action relief provided herein, in its discretion.

If you have any questions concerning this correspondence, please contact Nancy Markowitz, Deputy Director, Division of Market Oversight, at (202) 418-5453 or [nmarkowitz@cftc.gov](mailto:nmarkowitz@cftc.gov), or Lois Gregory, Associate Director, Division of Market Oversight, at (202) 418-5569 or [lgregory@cftc.gov](mailto:lgregory@cftc.gov).

Sincerely,



Vincent A. McGonagle  
Director  
Division of Market Oversight

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<sup>15</sup> See STP Guidance.

<sup>16</sup> The applicable swap data reporting requirements are set forth under parts 43, 45, and 50 of the Commission's regulations. The applicable clearing requirements are set forth under Commodity Exchange Act section 2(h)(1) and part 50 of the Commission's regulations. The applicable pre-execution credit check requirements are set forth under §1.73 of the Commission's regulations. The applicable straight-through processing requirements are set forth under §1.74, §37.702(b), and §39.12(b)(7) of the Commission's regulations.