

## COMMODITY FUTURES TRADING COMMISSION

### 17 CFR Parts 1, 150 and 151

RIN 3038-AD15 and 3038-AD16

### Position Limits for Derivatives

**AGENCY:** Commodity Futures Trading Commission.

**ACTION:** Notice of proposed rulemaking.

**SUMMARY:** Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank Act”) requires the Commodity Futures Trading Commission (“Commission” or “CFTC”) to establish position limits for certain physical commodity derivatives. The Commission is proposing to simultaneously establish position limits and limit formulas for certain physical commodity futures and option contracts executed pursuant to the rules of designated contract markets (“DCM”) and physical commodity swaps that are economically equivalent to such DCM contracts. In compliance with the requirements of the Dodd-Frank Act, the CFTC is also proposing aggregate position limits that would apply across different trading venues to contracts based on the same underlying commodity. The Commission is proposing to establish position limits in two phases: The first phase would involve adopting current DCM spot-month limits, while the second phase would involve establishing non-spot-month limits based on open interest levels as well as establishing Commission-determined spot-month limits. The proposal includes exemptions for *bona fide* hedging transactions and for positions that are established in good faith prior to the effective date of specific limits that could be adopted pursuant to final regulations. This notice of rulemaking also proposes new account aggregation standards, visibility regulations that are similar to current reporting obligations for large *bona fide* hedgers, and new regulations establishing requirements and standards for position limits and accountability rules that are implemented by registered entities. The Commission solicits comment on any aspect of the proposal. The Commission also solicits comment on particular issues throughout the preamble.

**DATES:** Comments must be received on or before March 28, 2011.

**ADDRESSES:** You may submit comments, identified by RIN numbers 3038-AD15 and 3038-AD16, by any of the following methods:

- Agency Web site, via its Comments Online process: <http://>

[comments.cftc.gov](http://comments.cftc.gov). Follow the instructions for submitting comments through the Web site.

- **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 instructions for submitting comments.

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](http://www.cftc.gov). You should submit only information that you wish to make available publicly. If you wish the Commission to consider information that 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 procedure established in § 145.9 of the Commission’s regulations (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 <http://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:** Stephen Sherrod, Acting Deputy Director, Market Surveillance, (202) 418-5452, [ssherrod@cftc.gov](mailto:ssherrod@cftc.gov), or Bruce Fekrat, Senior Special Counsel, Office of the Director, (202) 418-5578, [bfekrat@cftc.gov](mailto:bfekrat@cftc.gov), Division of Market Oversight, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW., Washington, DC 20581.

#### SUPPLEMENTARY INFORMATION:

#### I. Position Limits for Physical Commodity Futures and Swaps

##### A. Background

The Commodity Exchange Act (“CEA” or “Act”) of 1936,<sup>1</sup> as amended by Title VII of the Dodd-Frank Act,<sup>2</sup> includes

<sup>1</sup> 7 U.S.C. 1 *et seq.*

<sup>2</sup> See Dodd-Frank Wall Street Reform and Consumer Protection Act, Public Law 111-203, 124 Stat. 1376 (2010). The text of the Dodd-Frank Act may be accessed at <http://www.cftc.gov/LawRegulation/OTCDERIVATIVES/index.htm>.

provisions imposing clearing and trade execution requirements on standardized derivatives as well as comprehensive recordkeeping and reporting requirements that extend to all swaps, as defined in CEA section 1a(47). Newly amended section 4a(a)(1) of the Act authorizes the Commission to extend position limits beyond futures and option contracts to swaps traded on a DCM or swap execution facility (“SEF”), swaps that are economically equivalent to DCM futures and option contracts with position limits, and swaps not traded on a DCM or SEF that perform or affect a significant price discovery function (“SPDF”) with respect to regulated entities. Further, new section 4a(a)(5) of the Act requires aggregate position limits for swaps that are economically equivalent to DCM futures and option contracts with CFTC-set position limits. Similarly, new section 4a(a)(6) of the Act requires the Commission to apply position limits on an aggregate basis to contracts based on the same underlying commodity across: (1) DCMs; (2) with respect to foreign boards of trade (“FBOTs”), contracts that are price-linked to a DCM or SEF contract and made available from within the United States via direct access; and (3) SPDF swaps.

Sections 4a(a)(2)(B) and 4a(a)(3) of the Act charge the Commission with setting spot-month, single-month and all-months-combined limits for DCM futures and option contracts on exempt and agricultural commodities<sup>3</sup> within 180 and 270 days, respectively, of the Dodd-Frank Act’s enactment.<sup>4</sup> In this notice of rulemaking, the Commission is proposing to establish limits required by Congress in amended CEA section 4a in two phases, which could involve multiple final regulations or different implementation dates.<sup>5</sup> In the first

<sup>3</sup> Section 1a(20) of the Act defines the term “exempt commodity” to mean a commodity that is not an excluded commodity or an agricultural commodity. Section 1a(19) defines the term “excluded commodity” to mean, among other things, an interest rate, exchange rate, currency, credit risk or measure, debt or equity instrument, measure of inflation, or other macroeconomic index or measure. Although the term “agricultural commodity” is not defined in the Act, CEA section 1a(9) enumerates a non-exclusive list of agricultural commodities. The Commission issued a notice of rulemaking proposing a definition for the term “agricultural commodity” on October 26, 2010. 75 FR 65586. Although broadly defined, exempt commodity futures contracts are often viewed as energy and metals products.

<sup>4</sup> Section 737 of the Dodd-Frank Act, which amended section 4a of the Act, became effective on July 21, 2010.

<sup>5</sup> The Commission may implement the two phases in various ways. It may, for example, pursuant to this notice of proposed rulemaking, adopt a single final regulation with two implementation provisions, or it may adopt two separate final regulations.

transitional phase the Commission proposes to establish spot-month position limits at the levels currently imposed by DCMs. This first phase would include related provisions, such as proposed regulation 151.5, pertaining to *bona fide* hedging, and proposed § 151.7, pertaining to account aggregation standards. During the second phase the Commission proposes to establish single-month and all-months-combined position limits and to set Commission-determined spot-month position limits.

As discussed in further detail below, phased implementation is possible because spot-month position limits are based on available information: DCMs currently set spot-month position limits based on their own estimates of deliverable supply. Spot-month limits can, therefore, be implemented by the Commission relatively expeditiously. In contrast, most non-spot-month position limits, as set by the Commission previously and as proposed herein, are based on open interest levels. Because the Commission was barred under the Commodity Futures Modernization Act of 2000 from collecting regular data or regulating most swaps markets, the Commission does not currently have the open interest and market structure data necessary to establish non-spot-month position limits. The Commission has proposed regulations that would permit it to gather positional data on physical commodity swaps on a regular basis.<sup>6</sup>

Because the Commission will not be able to implement a comprehensive system for gathering swap positional data for some time, this notice of proposed rulemaking does not propose to determine the numerical non-spot-month position limits for exempt and agricultural commodity derivatives resulting from the application of the open interest formulas in proposed § 151.4. Rather, this notice of rulemaking provides for the determination of such limits when the Commission receives data regarding the levels of open interest in the swap markets to which these limits will apply.

The Commission anticipates fixing initial position limits pursuant to the formulas proposed herein through the issuance of a Commission order. As proposed, CFTC-set position limits after the transitional period would be recalculated every year based on the formulas set forth in proposed § 151.4, subject to any changes to the formulas

that may be proposed and adopted based on the Commission's surveillance of the markets for referenced contracts. In this regard, as discussed in further detail below, the proposed position visibility regulations, which would effectuate reporting requirements that are similar to current reporting requirements for large *bona fide* hedgers, may facilitate evaluating the efficacy and appropriateness of the proposed position limit framework if adopted.

#### B. Statutory Authority

##### 1. Section 4a of the Act

The Dodd-Frank Act preserves the Commission's broad authority to set position limits. Thus, for example, section 4a(a)(1) of the Act expressly permits the Commission to set "different limits for, among other things, different commodities, markets, futures, or delivery months \* \* \*" Under new CEA section 4a(a)(7), the Commission also has authority to exempt persons or transactions from any position limits it establishes.

New section 4a(a)(3) of the Act expressly directs the Commission to set such limits at levels that would serve, to the maximum extent practicable, in its discretion:

- (i) To diminish, eliminate, or prevent excessive speculation as described under this section;
- (ii) To deter and prevent market manipulation, squeezes, and corners;
- (iii) To ensure sufficient market liquidity for *bona fide* hedgers; and
- (iv) To ensure that the price discovery function of the underlying market is not disrupted.<sup>7</sup>

This provision incorporates the Commission's historical approach to setting limits, and is harmonious with the congressional directive in section 4a(a)(1) of the Act that the Commission set position limits to prevent or minimize price disruptions that could be caused by excessive speculative trading.

Section 4a(a)(5) of the Act requires the Commission to develop, concurrently with position limits for DCM futures and option contracts, position limits for swaps that are economically equivalent to such contracts. Section 4a(a)(5) of the Act requires such position limits, when developed, to be adopted simultaneously.<sup>8</sup> The defined term

"referenced contract" in proposed § 151.1, through its reference to the core futures contracts listed in proposed § 151.2 ("core referenced futures contracts" or "151.2-listed contract"), identifies the "economically equivalent" derivatives that would be subject to the concurrent development, simultaneous establishment and aggregate implementation requirements of CEA section 4a. Referenced contracts are defined as derivatives (1) that are directly or indirectly linked to the price of a 151.2-listed contract, or (2) that are based on the price of the same commodity for delivery at the same location(s) as that of a 151.2-listed contract, or another delivery location with substantially the same supply and demand fundamentals as the delivery location of a 151.2-listed contract.<sup>9</sup> The second part of the definition of referenced contract therefore proposes to include derivatives that are settled to a price series that is not based on, but is nonetheless highly correlated to, the price of a 151.2-listed contract. Proposed § 151.2, in turn, enumerates 28 core physical delivery DCM futures contracts that would be subject to the Commission's proposed position limit framework. Generally, the 151.2-listed contracts were selected either because such contracts have high levels of open interest and significant notional value or because they otherwise may provide a reference price for a significant number of cash market transactions.<sup>10</sup>

A primary mission of the CFTC is to foster fair, open and efficient functioning of the commodity derivatives markets.<sup>11</sup> Critical to fulfilling this statutory mandate is protecting market users and the public from undue burdens that may result from "excessive speculation." Specifically, section 4a of the Act, as amended by the Dodd-Frank Act, provides that:

"Excessive speculation in any commodity under contracts of sale of such commodity for future delivery [(or swaps traded on or subject to the rules of a designated contract market or swap execution facility, or swaps that perform a significant price discovery function with respect to a registered entity)] \* \* \* causing sudden or unreasonable fluctuations or unwarranted changes in the price of such commodity, is an undue and unnecessary burden on interstate commerce in such commodity. For the purpose of diminishing, eliminating, or preventing such

notice of rulemaking a process by which swaps that perform or affect a significant price discovery function with respect to regulated entities can be identified.

<sup>9</sup> 75 FR 67258, at 67260 (discussing the scope of directly and indirectly linked swaps).

<sup>10</sup> See 75 FR 67258, at 672758.

<sup>11</sup> See section 3 of the Act, 7 U.S.C. 5.

<sup>7</sup> 7 U.S.C. 6a(a)(3).

<sup>8</sup> Unlike swaps that are economically equivalent to DCM futures and option contracts with position limits, the Commission is not required to develop or establish position limits for SPDF swaps at the same time that it develops or establishes position limits for DCM futures and option contracts. The Commission intends to propose in a subsequent

<sup>6</sup> See *Position Reports for Physical Commodity Swaps*, 75 FR 67258, November 2, 2010 (proposing position reports on economically equivalent swaps from clearing organizations, their members and swap dealers).

burden, the Commission shall \* \* \* proclaim and fix such limits on the amount of trading which may be done or positions which may be held by any person \* \* \* as the Commission finds are necessary to diminish, eliminate or prevent such burden. \* \* \*<sup>12</sup>

Congress has declared that sudden or unreasonable price fluctuations attributable to “excessive speculation” create an “undue and unnecessary burden” on interstate commerce and directed that the Commission shall establish limits on the amounts of positions which may be held as it finds necessary to “diminish, eliminate, or prevent” such burden. As the plain reading of the statutory text indicates, the prevention of sudden or unreasonable changes in price attributable to large speculative positions, even without manipulative intent, is a congressionally-endorsed regulatory objective of the Commission.

The Commission is not required to find that an undue burden on interstate commerce resulting from excessive speculation exists or is likely to occur in the future in order to impose position limits. Nor is the Commission required to make an affirmative finding that position limits are necessary to prevent sudden or unreasonable fluctuations or unwarranted changes in prices or otherwise necessary for market protection. Rather, the Commission may impose position limits prophylactically, based on its reasonable judgment that such limits are necessary for the purpose of “diminishing, eliminating, or preventing” such burdens on interstate commerce that the Congress has found result from excessive speculation. A more restrictive reading would be contrary to the congressional findings and objectives as embodied in section 4a of the Act.<sup>13</sup>

<sup>12</sup> Section 4a(a)(1) of the Act, 7 U.S.C. 6a(a)(1).

<sup>13</sup> Consistent with the congressional findings and objectives, the Commission has previously set position limits without finding that an undue burden of interstate commerce has occurred or is likely to occur, and in so doing has expressly stated that such additional determinations by the Commission were not necessary in light of the congressional findings in section 4a of the Act. In its 1981 rulemaking to require all exchanges to adopt position limits for commodities for which the Commission itself had not established limits, the Commission stated:

“As stated in the proposal, the prevention of large and/or abrupt price movements which are attributable to the extraordinarily large speculative positions is a congressionally endorsed regulatory objective of the Commission. Further, it is the Commission’s view that this objective is enhanced by the speculative position limits since it appears that the capacity of any contract to absorb the establishment and liquidation of large speculative positions in an orderly manner is related to the relative size of such positions, *i.e.*, the capacity of the market is not unlimited.”

## 2. Legislative History and Discussion

The relevant legislative history, including the congressional debates and studies preceding the enactment of the CEA, gives further evidence to the broad mandate conferred on the Commission pursuant to CEA section 4a. Throughout the 1920s and into the 1930s, a series of studies and reports found that large speculative positions in the futures markets for grain, even without manipulative intent, can cause “disturbances” and “wild and erratic” price fluctuations. To address such market disturbances, Congress was urged to adopt position limits to restrict speculative trading notwithstanding the absence of “the deliberative purpose of manipulating the market.”<sup>14</sup> In 1936, based upon such reports and testimony, Congress provided the Commodity Exchange Authority (the predecessor of the Commission) with the authority to impose Federal speculative position limits. In doing so, Congress expressly acknowledged the potential for market disruptions resulting from excessive speculative trading and the need for

*Establishment of Speculative Position Limits*, 46 FR 50938, Oct. 16, 1981 (adopting then regulation 1.61 (now part of regulation 150.5)).

<sup>14</sup> See 7, U.S. Fed. Trade Commission, Report of the Federal Trade Commission on the Grain Trade: Effects of Future Trading 293–94 (1926). For example, the Federal Trade Commission concluded:

The very large trader by himself may cause important fluctuations in the market. If he has the necessary resources, operations influenced by the idea that he has such power are bound to cause abnormal fluctuations in prices. Whether he is more often right than wrong and more often successful than unsuccessful, and whether influenced by a desire to manipulate or not, if he is large enough he can cause disturbances in the market which impair its proper functioning and are harmful to producers and consumers.

The FTC recommended that limits be placed on trading, particularly on the amount of open interest that could be held by any one trader. Similarly, based on its study of price fluctuations in the wheat market, the Department of Agriculture urged Congress to provide the Grain Futures Administration (GFA), which had been created by the Grain Futures Act, with the authority to impose position limits. See *Fluctuations in Wheat Futures*, S. Doc. No. 69–135 (1st Sess. 1926); see also *Speculative Position Limits in Energy Futures Markets: Hearing Before the U.S. Commodity Futures Trading Commission* (July 28, 2009) (statement of Dan M. Berkovitz, General Counsel, U.S. Commodity Futures Trading Commission), available at <http://www.cftc.gov/PressRoom/SpeechesTestimony/2009/berkovitzstatement072809.html>.

<sup>15</sup> The report accompanying the 1935 bill that became the Act stated “the fundamental purposes of the measure is to insure fair practice and honest dealing on the commodity exchanges and to provide a measure of control over those forms of speculative activity which too often demoralize the markets to the injury of producers and consumers and the exchanges themselves. H.R. Rep. No. 74–421, at 1 (1935), accompanying H.R. 6772.

measures to prevent or minimize such occurrence.<sup>15</sup>

The basic statutory mandate in section 4a of the Act to establish position limits to prevent “undue burdens” associated with “excessive speculation” has remained unchanged—and has been reaffirmed by Congress several times—over the past seven decades. In 1974, when Congress created the Commission as an independent regulatory agency, it reiterated the purpose of the Act to prevent fraud and manipulation and to control speculation.<sup>16</sup> In connection with another major overhaul of the Act, the Commodity Futures Modernization Act of 2000, Congress expressly authorized exchanges to use position accountability as an alternative means to limit speculative positions. However, Congress did not alter the Commission’s mandate in CEA section 4a to establish position limits to prevent such undue burdens on interstate commerce. Then, in the CFTC Reauthorization Act of

<sup>14</sup> See 7, U.S. Fed. Trade Commission, Report of the Federal Trade Commission on the Grain Trade: Effects of Future Trading 293–94 (1926). For example, the Federal Trade Commission concluded:

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<sup>16</sup> S. Rep. No. 93–1131, 93rd Cong., 2d Sess. (1974).

2008,<sup>17</sup> Congress, among other things, expanded the Commission's authority to set position limits to significant price discovery contracts on exempt commercial markets.

Finally, as outlined above, pursuant to the Dodd-Frank Act, Congress significantly expanded the Commission's authority and mandate to establish position limits beyond futures and option contracts to include, for example, economically equivalent derivatives.<sup>18</sup> Congress expressly directed the Commission to set limits in accordance with the standards set forth in sections 4a(a)(1) and 4a(a)(3) of the Act,<sup>19</sup> thereby reaffirming the Commission's authority to establish position limits as it finds necessary in its discretion to address excessive speculation.<sup>20</sup> As noted earlier, section 4a(a)(3) of the Act expressly sets forth the Commission's broad discretion in setting position limits under section 4a(a)(1), and the necessary considerations in setting such limits. Section 4a(a)(3) effectively incorporates the Commission's historical approach to setting limits,<sup>21</sup> and is harmonious with the congressional directive in section 4a(a)(1) of the Act that the Commission set position limits in its discretion to prevent or minimize burdens that could be caused by excessive speculative trading.

Large concentrated positions in the physical commodity markets can potentially facilitate price distortions given that the capacity of any market to absorb the establishment and liquidation of large positions in an orderly manner is related to the size of such positions relative to the market and the market's structure and is, therefore, not unlimited.<sup>22</sup>

<sup>17</sup> Food, Conservation and Energy Act of 2008, Public Law 110-246, 122 Stat. 1624 (June 18, 2008).

<sup>18</sup> Dodd-Frank Act, Public Law 111-203, 737, 124 Stat. 1376 (2010). The Dodd-Frank Act amendments to section 4a of the Act became effective upon the date of enactment of the Dodd-Frank Act.

<sup>19</sup> Section 4a(a)(2) of the Act provides that the Commission, in setting position limits, must do so in accordance with the standards set forth in CEA section 4a(a)(1). 7 U.S.C. 6a(a)(2).

<sup>20</sup> Senator Lincoln (then the Chair to the Senate Agriculture Committee) stated that amended section 4a "will grant broad authority to the [Commission] to once and for all set aggregate position limits across all markets on non-commercial market participants \* \* \* I believe the adoption of aggregate position limits will help bring some normalcy back to our markets and reduce some of the volatility we have witnessed over the last few years." 156 Cong. Rec. S5919 (daily ed. July 15, 2010) (statement of Sen. Lincoln).

<sup>21</sup> See 46 FR 50938.

<sup>22</sup> See *Fluctuations in Wheat Futures*, S. Doc. No. 69-135 (1st Sess. 1926); and 7 U.S. Fed. Trade Commission, *Report of the Federal Trade Commission on the Grain Trade: Effects of Future Trading* 293-94 (1926); see also Thomas A.

Concentration of large positions in one or a few traders' accounts can also create the unwarranted appearance of appreciable liquidity and market depth which, in fact, may not exist. Trading under such conditions can result in sudden changes to commodity prices that would otherwise not prevail if traders' positions were more evenly distributed among market participants.<sup>23</sup> Position limits address these risks through ensuring the participation of a minimum number of traders that are independent of each other and have different trading objectives and strategies.

The Commission currently sets and enforces position limits with respect to certain agricultural products. For metals and energy commodities, in 1981 the Commission began to require exchange-set limits, with a Commission approval process, for any active futures markets without existing Commission or exchange limits.<sup>24</sup> This framework was significantly scaled back in 1991, after which the Commission began to approve exchange accountability provisions in place of position limits.<sup>25</sup> Such accountability provisions took effect with respect to certain metals derivatives in 1992, and with respect to energy and soft agricultural derivatives in 2001. Currently, the Commission authorizes DCMs to set position limits and accountability rules to protect against manipulation and congestion and price distortions. The proliferation of economically-equivalent instruments trading in multiple trading venues,

Hieronimus, *Economics of Futures Trading* 313 (1971) ("Limits on speculative positions have met with a high degree of trade acceptance and only recently has the size of some of the limits begun to be called into question. The general notion is that no one man should be allowed to have such a position or trade in such volume that he could push the price around with his sheer bulk").

<sup>23</sup> By way of illustration, after the silver futures market crisis during late 1979 to early 1980, commonly referred to as "the Hunt Brothers silver manipulation," the Commission concluded that "[t]he recent events in silver suggest that the capacity of any futures market to absorb large positions in an orderly manner is not unlimited." Subsequently, the Commission adopted regulation 1.61, which required all exchanges to adopt and submit for Commission approval position limits in active futures markets for which no exchange or Commission limits were then in effect. More recently, Congress, in response to high prices and volatility in commodity prices generally, and energy prices in particular, extended the Commission's authority to set limits to significant price discovery contracts traded on exempt commercial markets. Food, Conservation and Energy Act of 2008, Public Law 110-246, 122 Stat. 1624 (June 18, 2008).

<sup>24</sup> 46 FR 50938.

<sup>25</sup> See *Speculative Position Limits—Exemptions from Commission Rule 1.61*, 56 FR 51687, October 15, 1991; and *Speculative Position Limits—Exemptions from Commission Rule 1.61*, 57 FR 29064, June 30, 1992.

however, warrants extension of the Commission-set position limits beyond agricultural products to metals and energy commodities. The Commission anticipates that this market trend will continue as, consistent with the regulatory structure established by the Dodd-Frank Act, economically equivalent derivatives based on exempt and agricultural commodities are executed pursuant to the rules of multiple DCMs and SEFs and other Commission registrants. Under these circumstances, uniform position limits should be established across such venues to prevent regulatory arbitrage and ensure a level playing field for all trading venues. Because it has the authority to gather data and impose regulations across trading venues, the Commission is uniquely situated to establish uniform position limits and related requirements for all economically equivalent derivatives.<sup>26</sup> A uniform approach would also encourage better risk management and could reduce systemic risk. Despite centralized clearing arrangements employed by DCMs to reduce systemic risk, a levered market participant can still take a very large speculative position across multiple venues. The proposed position limit framework would reduce the ability of such levered entities to take such positions and to cause systemic risk.

As noted above, in setting position limits to guard against excessive speculation, the Commission, pursuant to the factors enumerated in section 4a(a)(3) of the Act, has endeavored to maximize the objectives of preventing excessive speculation, deterring and preventing market manipulation, and ensuring that markets remain sufficiently liquid so as to afford end users and producers of commodities the ability to hedge commercial risks and to promote efficient price discovery.

### C. Public Comments in Advance of Commission Action

As with other forthcoming notices of rulemaking proposing regulations to implement the Dodd-Frank Act, the Commission accepted public comments in advance of issuing this release. The Commission has received approximately 350 public comments as of December 16, 2010.<sup>27</sup> The Commission has reviewed these comments and considered them in drafting the

<sup>26</sup> Because individual markets have knowledge of positions on their own facilities, it is difficult for them to assess the full impact of a trader's positions on the greater market.

<sup>27</sup> These comments may be accessed at [http://www.cftc.gov/LawRegulation/DoddFrankAct/OTC\\_26\\_PosLimits.html](http://www.cftc.gov/LawRegulation/DoddFrankAct/OTC_26_PosLimits.html).

proposed regulations. The majority of commenters submitted letters advocating the view that position limits should be set at one percent of the total annual world production for a given commodity. Several expressed views on a single issue, notably the importance of preventing market manipulation.

The view most commonly expressed by certain other commenters, including the CME Group, Electric Power Supply Association, Futures Industry Association, Morgan Stanley, and National Gas Supply Association, was opposition to a provision that resulted in the “crowding out” of speculative positions. A “crowding out” provision would have limited the ability of a trader that hedges or acts as a swap dealer to take on speculative positions once certain positional thresholds were exceeded.<sup>28</sup> A concern raised by the commenters was related to the unintended consequence of excluding knowledgeable traders, or traders that needed to hold speculative positions, from the commodity derivatives markets. The Commission has determined to not propose a “crowding out” provision at this time.

Several commenters addressed *bona fide* hedging exemptions to position limits. Some of these commenters, for example the CME Group, presented the view that the Commission should adopt a broad definition for *bona fide* positions that would cover “all non-speculative” positions. Morgan Stanley recommended that the Commission “exercise its discretion to interpret [s]ection 4(a)(c)(2), including the term ‘economically appropriate’, broadly to permit products and services similar to [risk management products offered by swap dealers] to qualify as *bona fide* hedging transactions or positions.” The National Grain and Feed Association (“NGFA”) presented the view that the Commission “should use its authority to grant hedge exemptions to financial institutions, index funds, hedge funds or other nontraditional participants in agricultural futures markets extremely sparingly and only if it can be demonstrated clearly that such exemptions will not harm contract performance for traditional hedgers.” The NGFA further recommended that the Commission “‘look through’ swap transactions and allow hedge exemptions to be granted only for that portion of swap dealers’ business where the swap dealers’ counterparties are entities that otherwise would have

qualified for a hedge exemption.” The Commission has seriously considered these views on the *bona fide* hedging exemption in light of the express language of the Act. The Commission has accordingly determined to propose a definition of *bona fide* hedging in proposed § 151.5(a)(1)(iv) that provides for an exemption for a non-*bona fide* swap counterparty only if such swap transaction or position represents cash market transactions and offsets its *bona fide* counterparty’s cash market risks.

Several commenters, including the CME Group, Electric Power Supply Association, Futures Industry Association, GDF Suez Energy, Morgan Stanley, and NextEra Energy Power Marketing, expressed concerns relating to the potential for overly strict account aggregation standards. The aggregation standards of the proposed regulations attempt to address some of these concerns by including exemptions for passive investments in independently controlled and managed commercial entities as well as exemptions for certain positions held with futures commission merchants and for traders that are passive pool participants. The law firm Akin Gump Strauss Hauer & Feld LLP, on behalf of a commodity trading advisor, specifically argued for the retention of the independent account controller exemption currently in force in part 150 of the Commission’s regulations, echoing the views of numerous commenters to the January 2010 proposed rulemaking for position limits on certain energy contracts. As explained in more detail in the aggregation section of this preamble, the proposed regulations address the concern of not having an independent account controller exemption by establishing the owned non-financial entity exemption. Some commenters, for example the Electric Power Supply Association, Futures Industry Association and Morgan Stanley, argued that aggregation should be based solely on common control, with no consideration given to common ownership. At this time, the Commission does not see sufficient justification to change its longstanding approach of considering both control and ownership in its aggregation policy. The traditional ten percent ownership standard has proven to be a useful measure in conjunction with the control standard. In addition, the proposed owned non-financial entity exemption addresses situations in which the 10 percent ownership standard has been exceeded but a lack of common control over trading decisions and strategies warrants disaggregation.

The CME Group also argued that position limits should not be imposed until the Commission has gathered sufficient data on the physical commodity swap markets. In order to address similar concerns, the Commission proposed regulations in November 2010 that are specifically designed to gather positional data on physical commodity swaps.<sup>29</sup> The Commission anticipates the collection of positional data to begin during the third quarter of 2011. Furthermore, the Commission is proposing to fix specific position limits pursuant to formulas proposed herein (and making other aspects of the proposed regulations effective) only after collecting positional data on physical commodity swaps and through the issuance of a Commission order during the first quarter of 2012, unless the Commission determines that there are certain commodities for which data is sufficient to implement limits sooner.

In addition to review and consideration of public comments, Commission staff has held 32 meetings with a variety of market participants, including *bona fide* hedgers, swap dealers, hedge funds and several industry groups, to discuss position limits and in particular to gather information about the potential impact of limits.<sup>30</sup> The Commission has considered information obtained in these meetings in drafting the proposed regulations.

## II. The Proposed Regulations

### A. Spot-Month Position Limits

The Commission proposes definitions in § 151.3 that identify the spot month<sup>31</sup> for referenced contracts in the same commodity that would be subject to the proposed position limit framework. These definitions reference the dates on which a spot month commences and terminates. The definitions for the spot period are based on existing spot-month definitions set forth by DCMs for 151.2-listed contracts. These periods, as defined by the Commission, would

<sup>29</sup> See 75 FR 67258.

<sup>30</sup> The Commission has made public all meetings that Commission staff has held with outside organizations in connection with the implementation of the Dodd-Frank Act, including, for each meeting, a list of attendees and a summary of the meeting. This information may be accessed at [http://www.cftc.gov/LawRegulation/DoddFrankAct/ExternalMeetings/otc\\_meetings.html](http://www.cftc.gov/LawRegulation/DoddFrankAct/ExternalMeetings/otc_meetings.html).

<sup>31</sup> The term “spot month” does not refer to a month of time. Rather, it is the trading period immediately preceding the delivery period for a physically-delivered futures contract and cash-settled swaps and futures contracts that are linked to the physically-delivered contract. The length of this period may thus vary depending on the referenced contract, as described in proposed regulation 151.3.

<sup>28</sup> See *Federal Speculative Position Limits for Referenced Energy Contracts and Associated Regulations*, 75 FR 4144, at 4146, January 26, 2010, withdrawn 75 FR 50950, August 18, 2010.

continue into the delivery period for the core referenced futures contracts, which in turn determine the spot month for all referenced contracts in the same commodity.

With three exceptions, the 151.2-listed contracts with DCM-defined spot months are currently subject to exchange-set spot-month position limits.<sup>32</sup> Proposed § 151.4 would impose and aggregately apply spot-month position limits for the referenced contracts. Consistent with the Commission's longstanding policy regarding the appropriate level of spot-month limits for physical delivery contracts, these position limits would be set at 25 percent of estimated deliverable supply. The spot-month limits would be adjusted annually thereafter.

The proposed deliverable supply formula narrowly targets the trading that may be most susceptible to, or likely to facilitate, price disruptions. The formula seeks to minimize the potential for corners and squeezes by facilitating the orderly liquidation of positions as the market approaches the end of trading and by restricting the swap positions which may be used to influence the price of referenced contracts that are executed centrally. Referenced contracts that are based on the price of the same commodity but where delivery is at a location that is different than the delivery location of a 151.2-listed contract would not be subject to the proposed Federal spot-month position limit. Because the potential incentive and ability to manipulate the spot-month delivery process to benefit a derivatives position providing for delivery at a different delivery location is less, Federal spot-month limits would apply only to futures, options and swaps that are directly price-linked to a 151.2-listed core referenced contract or that settle to a price series that prices the same commodity at the same delivery location. Finally, the proposed spot-month limits would apply on an aggregate basis, thereby subjecting these economically equivalent derivatives to the same spot-month limits, whether or not they are listed for trading on a DCM, cleared, or uncleared.

Proposed § 151.4 would apply spot-month position limits separately for physically-delivered contracts and all

cash-settled contracts, including cash-settled futures and swaps. A trader may therefore have up to the spot-month position limit in both the physically-delivered and cash-settled contracts. For example, if the spot-month limit for a referenced contract is 1,000 contracts, then a trader may hold up to 1,000 contracts long in the physically-delivered contract and 1,000 contracts long in the cash-settled contract. A trader's cash-settled contract position would separately be a function of the trader's position in referenced contracts based on the same commodity that are cash-settled futures and swaps.<sup>33</sup>

The proposed spot-month position limit formula is based on the Commission's longstanding approach to setting and overseeing spot-month limits and is consistent with industry practice and the goals of preventing manipulation through corners or squeezes. Core Principles 3 and 5 for DCMs address congressional concerns regarding potential manipulation of the futures market, and the Commission has typically evaluated compliance with these core principles in tandem. Core Principle 3 specifies that a board of trade shall list only contracts that are not readily susceptible to manipulation, while Core Principle 5 obligates a DCM to establish position limits and position accountability provisions where necessary and appropriate "to reduce the threat of market manipulation or congestion, especially during the delivery month."

In determining whether a physical delivery contract complies with Core Principle 3, the Commission considers whether the specified terms and conditions, considered as a whole, result in a deliverable supply that is sufficient to ensure that the contract is not conducive to price manipulation or distortion. In general, the term "deliverable supply" means the quantity of the commodity meeting a derivative contract's delivery specifications that can reasonably be expected to be readily available to short traders and saleable by long traders at its market value in normal cash marketing channels at the derivative contract's delivery points during the specified delivery period, barring abnormal movement in interstate commerce. The establishment of a spot-month limit pursuant to Core Principle 5 is made based on the analysis of deliverable supplies, and the

Acceptable Practices for this Core Principle state that, for physically delivered contracts, the spot-month limit should not exceed 25 percent of the estimated deliverable supply. Likewise, the guidance for DCMs in Commission § 150.5(b) provides that for physical delivery contracts, the spot-month limit level must be no greater than 25 percent of the estimated spot-month deliverable supply, calculated separately for each month to be listed.

In § 151.4, the Commission proposes spot-month limits, for not only referenced contracts that are futures but also referenced contracts that are economically equivalent swaps, that would, during the initial implementation period, be set at the spot-month limit levels determined by DCMs to be equal to 25 percent of estimated deliverable supply.<sup>34</sup> In the second phase of implementation, these spot-month limits would be based on 25 percent of estimated deliverable supply as determined by the Commission, which could choose to adopt exchange-provided estimates or, for example, in the case of inconsistent estimates from exchanges, issue its own estimates. Pursuant to current exchange procedures for updating the spot-month limits, exchanges initially establish and periodically update their limits through rule amendments that are filed with the Commission under self-certification or approval procedures. As part of the initial filing, or in response to subsequent inquiries from the Commission, the exchanges provide information showing how the spot-month limits comply with the Commission's regulations and acceptable practices.

With respect to the existing spot-month limits that currently are in effect for referenced contracts, the Commission notes that, irrespective of the manner in which a rule amendment is filed (by self-certification or for approval), Commission staff currently evaluates the limits for compliance with the requirements of Core Principle 5 and the criteria set out in the Commission's Acceptable Practices. For physically delivered contracts, staff evaluates the information supplied by the exchange and other available information regarding the underlying commodity to ensure that the spot-month limit does not exceed 25 percent of the estimated deliverable supplies. For cash-settled

<sup>32</sup> The only contracts based on a physical commodity that currently do not have spot-month limits are the COMEX mini-sized gold, silver, and copper contracts that are cash-settled based on the futures settlement prices of the physical-delivery contracts. The cash-settled contracts have position accountability provisions in the spot month rather than outright spot-month limits. These cash-settled contracts have relatively small levels of open interest.

<sup>33</sup> For purposes of applying the limits, a trader would convert and aggregate positions in swaps on a futures equivalent basis. Guidance on futures equivalency is provided in Appendix A to the Commission's proposed part 20 rulemaking on position reports for physical commodity swaps. 75 FR 67258, at 67269.

<sup>34</sup> For the ICE Futures U.S. Sugar No. 16 (SF) and Chicago Mercantile Exchange Class III Milk (DA), the Commission proposes to adopt the DCM single-month limits for the nearby month or first-to-expire referenced contract as spot-month limits. These contracts currently have single-month limits which are enforced in the spot month.

contracts, staff evaluates the information supplied by the exchanges and independently assesses the nature of the market underlying the cash-settlement calculation, including the depth and breadth of trading in that market, to determine the ability of a trader to exert market power and influence the cash-settlement price, with the aim of having a spot-month limit level that effectively limits a trader's incentive to exercise such market power.

With respect to cash-settled contracts, proposed § 151.4 incorporates a conditional-spot-month limit that permits traders without a hedge exemption to acquire position levels that are five times the spot-month limit if such positions are exclusively in cash-settled contracts and the trader holds physical commodity positions that are less than or equal to 25 percent of the estimated deliverable supply. The proposed limit maximizes the objectives, enumerated in section 4a(a)(3) of the Act, of deterring manipulation and excessive speculation while ensuring market liquidity and efficient price discovery by establishing a higher limit for cash-settled contracts as long as such positions are decoupled from large physical commodity holdings and the positions in physical delivery contracts which set or affect the value of cash-settled positions. The conditional-spot-month position limit generally tracks exchange-set position limits currently implemented for certain cash-settled energy futures and swaps. For example, the NYMEX Henry Hub Natural Gas Last Day Financial Swap, the NYMEX Henry Hub Natural Gas Look-Alike Last Day Financial Futures, and the ICE Henry LD1 swap are all cash-settled contracts subject to a conditional-spot-month limit that, with the exception of the requirement that a trader not hold large cash commodity positions, is identical in structure to the limit proposed herein.

This proposed conditional spot-month position limit formula is consistent with Commission guidance. The Acceptable Practices for Core Principle 5 state that a spot-month position limit may be necessary if the underlying cash market is small or illiquid such that traders can disrupt the cash market or otherwise influence the cash-settlement price to profit on a futures position. In these cases, the limit should be set at a level that minimizes the potential for manipulation or distortion of the futures contract or the underlying commodity's price. With respect to cash-settled contracts where the underlying product is a physical commodity with limited supplies where a trader can exert market power

(including agricultural and exempt commodities), the Commission has viewed the specification of a spot-month limit to be an essential term and condition of such contracts in order to ensure that they are not readily susceptible to manipulation, which is the Core Principle 3 requirement, and to satisfy the requirements of Core Principle 5 and the Acceptable Practices thereunder. In practice, for cash-settled contracts on agricultural and exempt commodities where a trader's market power is of concern, the practice has been to set the spot-month limit at some percentage of calculated deliverable supply. Limiting a trader's position at the expiration of cash-settled contracts diminishes the incentive to exert market power to manipulate the cash-settlement price or index to advantage a trader's position in the cash-settlement contract. Accordingly, the Commission has viewed the presence of a spot-month speculative limit as a key feature of such cash-settlement contracts, along with the design of the cash-settlement index, in ensuring that such contracts are not readily susceptible to manipulation and thus satisfy the requirements of Core Principles 3 and 5.

In view of the above, the Commission generally has required that, to comply with Core Principles 3 and 5, all futures contracts based on agricultural or exempt commodities, because they have finite supplies and are subject to price distortion and manipulation, must have a spot-month limits, irrespective of whether the contract specifies physical delivery or cash settlement. In addition, the establishment of position limits on swaps is consistent with congressional guidance in the CFTC Reauthorization Act of 2008.<sup>35</sup> That legislation amended the CEA by, among other things, adding core principles in new section 2(h)(7) governing swaps that were significant price discovery contracts traded on electronic trading facilities operating in reliance on the exemption in section 2(h)(3) of the Act. The 2008 legislation amended the Act to impose certain self-regulatory responsibilities with respect to such swaps through core principles, including a core principle that required the adoption of position limits or position accountability levels where necessary and appropriate. The CFTC Reauthorization Act, thus, recognized the appropriateness of treating certain swaps and futures contracts in the same manner, thereby authorizing the imposition of position limits on such

swaps (which are cash-settled contracts).

In order to facilitate the annual calculations of spot-month position limits, the Commission proposes to require each DCM that lists a referenced physical delivery contract to submit, on an annual basis, an estimate of deliverable supply to the Commission. This estimate would include supplies that are available through standard marketing channels at market prices prevailing during the relevant spot months. Deliverable supply would not include supplies that could be procured at unreasonably high prices or diverted from non-standard locations. Deliverable supply would also not include supply that is committed for long-term agreements and would therefore not be available to fulfill the delivery obligations arising from current trading. The Commission would consider the DCM's estimate in conjunction with analyzing its own data and reviewing position limit related DCM filings, and make a final determination as to deliverable supply. In making this determination, the Commission would weigh more heavily the highest monthly values of past deliverable supply, provided it did not occur in particularly unusual market conditions, over a reasonable time period to estimate the largest deliverable supply.

The Commission invites comments on all aspects of its proposed spot-month position limit framework. For example, how broadly or narrowly should the Commission consider what constitutes deliverable supply? Should the Commission adopt the proposed conditional-spot-month limits or adopt a uniform spot-month limit? Alternatively, should the conditional-spot-month limit be set at a higher level relative to the level of deliverable supply? If so, why?

#### *B. Non-Spot-Month Position Limits*

##### *1. Open Interest Formula*

While the Commission proposes to set spot-month limits in the transitional implementation period, the Commission would impose non-spot-month position limits only in the second phase of implementation. In contrast to spot-month position limits which are set as a function of deliverable supply, the class and aggregate single-month and all-months-combined position limits, as proposed, would be tied to a specific percentage of overall open interest for a particular referenced contract in the aggregate or on a per class basis. Under the proposed regulations, there are two classes of contracts in connection with

<sup>35</sup> Food, Conservation and Energy Act of 2008, Public Law 110-246, 122 Stat. 1624 (June 18, 2008).

non-spot-month limits. One class is comprised of all futures and option contracts executed pursuant to the rules of a DCM. The second class is comprised of all swaps.

In addition to an aggregate single-month and all-months-combined position limit that would apply across classes, the proposed regulations would apply single-month and all-months-combined position limits to each class separately. Class limits would ensure that market power is not concentrated in any one submarket, and that a trader is not flat in the aggregate while holding excessively large offsetting positions in any one submarket. Class and aggregate position limits based on a percentage of open interest may help prevent any single speculative trader from acquiring excessive market power. The formula proposed herein is intended to ensure that no single speculator can constitute more than 10 percent of a market, as measured by open interest, up to 25,000 contracts of open interest, and 2.5 percent thereafter.<sup>36</sup>

Proposed § 151.4 proposes to use the futures position limits formula (the 10, 2.5 percent formula) to determine non-spot-month position limits for referenced contracts. The 10, 2.5 percent formula is identified in current Commission § 150.5(c)(2). Given the level of open interest in the futures markets and the likely level of open swaps based on data available to the Commission, this formula would yield high position limits that nonetheless would prevent a speculative trader from acquiring excessively large positions and thereby would help prevent excessive speculation and deter and prevent market manipulation, squeezes, and corners. The resultant limits are purposely designed to be high in order to ensure sufficient liquidity for bona fide hedgers and avoid disrupting the price discovery process given the limited information the Commission has with respect to the size of the physical commodity swap markets.<sup>37</sup>

As discussed further below, for the agricultural futures contracts enumerated in current § 150.2, the Commission is proposing legacy limits that would retain the all-months-combined limits for such contracts and would make the single-month limits equal to the all-months-combined limits.

The Commission emphasizes that market data can support a range of

acceptable speculative position limits. The Commission currently obtains DCM futures and option positional data under parts 15 through 19 and 21 of its regulations, which derive their statutory authority in significant part from sections 4a, 4g and 4i of the CEA. With regard to swaps, the Commission receives limited positional data for cleared swaps that are significant price discovery contracts under part 36 of its regulations and limited positional data on certain swaps that are cleared, but not traded, by registered derivatives clearing organizations. While the Commission requires additional, reliable, and verifiable swaps data to enforce the position limits proposed herein, the Commission believes that it has sufficient data to set the overall concentration-based percentages for the position limits. The Commission intends to finalize regulations that would provide it with comprehensive positional data on physical commodity swaps, and would use such data to fix numerical position limits through the application of the proposed open-interest-based position limit formula.<sup>38</sup>

The trader visibility requirements of § 151.6, as described below, establish levels that trigger reporting requirements similar to reports that certain hedgers currently submit pursuant to '04 reports under part 19 of the Commission's regulations. These reporting requirements aim to make the physical and derivatives portfolios of the largest traders in referenced contracts visible to the Commission. This information would generally allow the Commission to understand large traders' trading activities and to assess the appropriateness of the speculative position limits set forth in the proposed part 151. The Commission would then potentially be able to, among other things, more readily identify instances where a trader's large positions create an ability to manipulate the market and cause sudden price changes or distortions. Moreover, the position visibility-related reports could potentially enable the Commission to perform some econometric analyses of the impact of speculative positions on price formation in referenced contracts. The position visibility levels that trigger reporting obligations are not intended to function as safe harbors from any charge of manipulation or excessive speculation. Visibility levels are in no way intended to imply that positions at or near such levels cannot constitute excessive speculation or be used to manipulate prices or for other wrongful purposes.

The Commission solicits comment as to whether the traditional 10, 2.5 percent formula should be uniformly applied to all referenced contracts as is being proposed. If not, why? In particular, given that single-month and all-months-combined position limits are not currently in place for energy and metals markets, should the Commission consider setting limits initially on these commodities at some higher level, such as a 10, 5 percent formula based on open interest, in order to best ensure that hedging activities or price discovery are not negatively affected? With respect to class limits, the Commission specifically solicits comment on whether additional classes, such as separate class categories for cleared and uncleared swaps, should be adopted to ensure that large positions that result in excessive concentration of positions in a submarket are not acquired?

## 2. Calculation of Open Interest

Under the proposed position limit framework, there are six possible non-spot-month position limits: *Aggregate* all-months-combined and single-month limits; *futures class* all-months-combined and single-month limits; and *swaps class* all-months-combined and single-month limits. In each case, single-month limits are proposed to equal all-months-combined limit levels. The Commission is proposing this approach in order to lessen the complexity of the limits and hence compliance burdens. The Commission is also proposing this approach, which would result in higher single-month limits, to incorporate a calendar spread exemption within the single-month limits (including an across crop year spread exemption) and remove the calendar spread exemption which would no longer be needed.

As discussed above, the Commission proposes to set non-spot-month position limits as a function of open interest. The general formula would set non-spot-month position limits as the sum of 10 percent of the first 25,000 contracts of open interest base and 2.5 percent of the open interest base beyond 25,000 contracts. All open interest base calculations would be derived from month-end open interest values. The open interest bases would be utilized to determine the average all-months-combined open interest which, in turn, would be the basis for the six non-spot-month position limits. Under proposed § 151.4(e), the average all-months-combined open interest would be the average of the relevant all-months open interest base for a calendar year. The open interest base levels would be

<sup>36</sup> See *Revision of Federal Speculative Position Limits*, 57 FR 12766, April 13, 1992; and *Revision of Federal Speculative Position Limits and Associated Rules*, 64 FR 24038, at 24039, May 5, 1999.

<sup>37</sup> See 57 FR 12766, at 12771.

<sup>38</sup> See 75 FR 67258.



calculated in the same manner described in the Commission’s January 2010 release proposing position limits for certain referenced energy contracts.<sup>39</sup>

Cleared referenced swap contract open interest would be based on month-end open interest figures provided to the Commission by clearing organizations. The Commission proposes to determine the uncleared swap open interest based on the month-end average for the sum of swap dealer positions in all months in uncleared referenced swap contracts. In order to determine a swap dealer’s position in all months in uncleared referenced swap

contracts, the Commission would undertake a four-step process. First, the Commission would determine a single swap dealer’s net exposure by counterparty by referenced contract month. Second, the Commission would add the swap dealer’s net counterparty exposures in the same referenced contract month on an absolute basis to determine the swap dealer’s open interest for the referenced contract single month. Third, the Commission would combine the swap dealer’s positions in the referenced contract month in order to determine its contribution to the uncleared swap single-month open interest. Finally, the

Commission would combine the swap dealer’s positions in single referenced contract months. At month end, this sum would constitute that swap dealer’s contribution to the uncleared referenced swap contract all-months open interest (and the aggregate all-months referenced contract open interest). For example, a swap dealer with the following referenced contract portfolio would contribute 2,000 contracts to the all-months uncleared swap open interest, 1,000 from each counterparty, based on positions of 1,100, 500, and 400 contracts for the January, February, and March referenced single contract months respectively:

	Net position January referenced contract	Net position February referenced contract	Net position March referenced contract
Counterparty 1 .....	- 600	- 200	- 200
Counterparty 2 .....	+500	- 300	- 200

3. Legacy Position Limits

The proposed regulations would retain the all-months-combined position limits for enumerated agricultural commodities in current § 150.2 as an exception to the general open interest based formula. The single-month limit would be increased to the same level as the legacy all-months-combined limit, with the elimination of the calendar month spread exemption.

The Commission requests comment on whether the legacy position limits should be retained or treated as other derivatives are treated under this proposal, and if so, whether the levels should be increased, to the following amounts requested in an April 6, 2010 petition to the Commission by the Chicago Board of Trade<sup>40</sup>:

Contract	Single month	All months
Corn (and Mini-Corn)	20,500	33,000
Soybeans (and Mini-Soybeans) .....	10,000	15,000
Wheat (and Mini-Wheat) .....	9,000	12,000
Soybean Oil .....	6,500	8,000

If so adopted, should the limits on wheat at the Minneapolis Grain Exchange and the Kansas City Board of Trade also be increased to the level proposed for the wheat contract at the

Chicago Board of Trade, consistent with the Commission’s historical approach to setting limits for wheat contracts?

C. Exemptions for Referenced Contracts

Proposed § 151.5 establishes exemptions from position limits for *bona fide* hedging transactions or positions as directed by the Dodd-Frank Act specifically for exempt and agricultural commodities. The referenced contracts subject to the proposed position limit framework would be subject to the *bona fide* provisions of proposed § 151.5 and would no longer be subject to § 1.3(z), which would be retained only for excluded commodities. § 1.47 and § 1.48 would be removed by this notice of proposed rulemaking.

Section 4a(c)(1) of the Act authorizes the Commission to define *bona fide* hedging transactions or positions “consistent with the purposes of the Act.” By its terms, the section places no restriction on the Commission’s ability to define *bona fide* hedging for swaps. Congress also directed the Commission, in amended CEA section 4a(c)(2), to adopt a definition for *bona fide* hedging transactions or positions for purposes of setting position limits pursuant to section 4a(a)(2), which refers only to futures contracts or options.<sup>41</sup> A definition of *bona fide* hedging that

would exclude swaps would deny a commercial end-user the option of offsetting price risks with swaps (as opposed to futures) pursuant to a *bona fide* hedge exemption. Accordingly, pursuant to section 4a(c)(1) and (c)(2), the Commission is proposing a definition for *bona fide* hedging transactions and positions that would apply to all referenced contracts, including swaps, as opposed to referenced futures and option contracts only.

The statutory definition of a *bona fide* hedge in section 4a(c)(2) generally follows the existing definition in Commission § 1.3(z)(1), except: (1) The directive requires all *bona fide* hedging transactions and positions to represent a substitute for a physical market transaction; and (2) as discussed above, the directive provides an explicit exemption for a trader to reduce the risks of swap positions, provided the counterparty to the swap transaction would have qualified for a *bona fide* hedging transaction exemption or the risk reducing positions offset a swap that qualifies as a *bona fide* hedging transaction.

The definition of *bona fide* hedging in § 1.3(z) of the Act provides that a *bona fide* hedging transaction or position in a futures contract normally represents a substitute for a physical market

<sup>39</sup> See 75 FR 4144, at 4153. A list of contracts that illustrate how open interest values would be calculated is available at [http://www.cftc.gov/LawRegulation/DoddFrankAct/Rulemakings/DF\\_26\\_PosLimits/index.htm](http://www.cftc.gov/LawRegulation/DoddFrankAct/Rulemakings/DF_26_PosLimits/index.htm). The list enumerates the types of referenced contracts’ open interest that would roll up into a 151.2-listed contract’s open interest for the purpose of determining overall open interest levels. Once swap open interest data for

swaps that are referenced contracts is collected, the open interest value for such swaps would also be rolled up into the related 151.2-listed futures contract’s open interest along with the open interest of other related referenced contracts.

<sup>40</sup> CME Group Petition for Amendment of Commodity Futures Trading Commission Regulation (April 6, 2010), available at <http://www.cftc.gov/LawRegulation/DoddFrankAct/>

*Rulemakings/DF\_26\_PosLimits/index.htm*. The CME petition was premised on the Commission’s past reliance on open interest levels for setting position limits and the increase in open interest levels of the contracts listed in the petition.

<sup>41</sup> The scope of contracts subject to position limits under section 4a(a)(2) includes physical commodity futures and options contracts traded on a DCM, other than excluded commodities.

transaction; thus, the current definition is no longer consistent with amended CEA section 4a(c)(2). The plain text of the new statutory definition of *bona fide* hedging recognizes *bona fide* hedging for derivatives that are subject to this rulemaking only if such transactions or positions represent cash market transactions and offset cash market risks, as opposed to the acceptance of *bona fide* hedging transactions and positions as activity that normally, but not necessarily, represents a substitute for cash market transactions or positions.

Proposed § 151.5(a)(2) incorporates the current requirements of Commission § 1.3(z)(2) for enumerated hedging transactions. Proposed § 151.5(a)(2)(iv) also provides an exemption for agents contractually responsible for the merchandising of cash positions with a person who owns the commodity or holds the cash market commitment being offset. This agent provision is consistent with Commission § 1.3(z)(3) and § 1.47.

In this regard, should the Commission grant an exemption to an agent that is not responsible for the merchandising of the cash positions, but is linked to the production of the physical commodity, for example, if the agent is the provider of crop insurance?

Proposed § 151.5(b) establishes reporting requirements for a trader upon exceeding a position limit. The trader is required to submit information not later than 9:00 a.m. on the business day following the day the limits were exceeded. The reports would support hedgers' need for large referenced contract positions and would give the Commission the ability to verify the positions were a *bona fide* hedge.

With respect to the frequency of filing such reports, should the Commission only require reports to be submitted either when a trader's position either first exceeds a limit or when a trader's hedging need increases, with a monthly summary while the trader's position remains in excess of the limit?

Proposed § 151.5(c) specifies application and approval requirements for traders seeking an anticipatory hedge exemption, incorporating the current requirements of Commission § 1.48. As is the case under current § 1.48, a trader's maximum sales and purchases shall not exceed the lesser of the approved exemption amount or the trader's current actual unsold anticipated production or current unfilled anticipated requirements. In addition, the proposed regulations require an anticipatory hedger to file a supplement to an application at least annually or whenever the anticipatory

hedging needs increase beyond that in the most recent filing.

Proposed § 151.5(d) establishes additional reporting requirements for a trader that exceeds the position limits to reduce the risks of certain swap transactions, discussed above. Should the Commission only require such reports to be submitted when the trader's position either first exceeds a limit or the hedging need increases, with a monthly summary while the trader's position remains in excess of the limit?

Proposed § 151.5(e) specifies recordkeeping requirements for traders that acquire positions in reliance on *bona fide* hedge exemptions, as well as for swap counterparties for which a counterparty represents that the transaction would qualify as a *bona fide* hedging transaction. Swap dealers availing themselves of a hedge exemption would be required to maintain a list of such counterparties and make that list available to the Commission upon request. Proposed § 151.5(g) and (h) provide procedural documentation requirements for such swap participants.

Proposed § 151.5(f) requires a cross hedger to provide conversion information, as well as an explanation of the methodology used to determine such conversion information, between the commodity exposure and the referenced contracts used in hedging.

Proposed § 151.5(i) requires reports by *bona fide* hedgers to be filed for each business day, up to and including the day after the trader's position level is below the position limit that was exceeded.

Proposed § 151.5(j) provides that a swap counterparty with respect to *bona fide* hedging transactions may establish a position in excess of the position limits, offset that position, and then re-establish a position in excess of the position limits. For example, this provision permits a swap participant who has reduced the risk of swaps using a position in futures contracts (that would otherwise violate a position limit) to offset those futures contracts and subsequently, if necessary, re-establish a position in excess of class position limits in another venue in order to once again reduce the risk of the swap transactions.

#### D. Position Visibility

Based on its analysis of the proposed limits as applied to futures and option contract positions and cleared swaps for which the Commission has open interest data, the Commission does not anticipate that the number of traders with positions in referenced base and

precious metals and referenced energy contracts, as further discussed below in the Cost-Benefit and Paperwork Reduction Act sections of this release, would constitute a significant segment of the affected markets, in contrast to the number of traders with positions in referenced agricultural contracts. Recognizing this, the Commission proposes to establish, in addition to the position limits discussed above, position visibility regulations for referenced contracts other than referenced agricultural contracts, pursuant to the Commission's authority to establish reporting requirements under section 4t of the Act, as added by the Dodd-Frank Act, and reporting requirements necessary for the establishment and enforcement of position limits under sections 4a and 8a(5) of the Act. The proposed visibility regulations would set position visibility reporting levels and establish reporting requirements for all traders exceeding those levels. The reporting regulations aim to make the physical and derivatives portfolios of the largest traders in referenced contracts visible to the Commission.

The position visibility regime would improve the Commission's ability to monitor the positions of the largest traders in the markets for referenced base and precious metals and referenced energy contracts and the effects on the markets of those large positions and their associated physical commodity and derivatives portfolios. The data for referenced contracts and related portfolios that the Commission would receive pursuant to the position visibility regulations would allow the Commission to better analyze the nature of the largest traders' positions in referenced contracts.

The Commission has set the visibility levels and its estimates on the number of traders they would capture based on data it currently receives on the futures and swaps markets. The Commission may revisit these levels as it begins to receive more data on the swaps markets. The Commission proposes to set the visibility reporting levels for referenced base and precious metals and referenced energy contracts where it anticipates approximately 20 unique owners over the course of a year would exceed such levels. Given their importance to the national economy, the Commission proposes to set visibility levels for the NYMEX Light Sweet Crude Oil (CL) and Henry Hub Natural Gas (NG) referenced contracts at a relatively lower level designed to capture approximately 30 unique owners over the course of a year.

Proposed § 151.6 would require traders with positions above visibility

levels in referenced base and precious metals and energy commodities to submit additional information about cash market and derivatives activity, including data relating to substantially the same commodity, such as commodities that are different grades or formulations of the same basic commodity. Proposed § 151.6(c) would require additional information, through a 402S filing, on a trader's uncleared swaps in substantially the same commodity. Proposed § 151.6(d) would require the reportable trader to submit information about cash market positions in substantially the same commodity, as described in proposed § 151.5(b), through 404 and 404A filings.

The Commission solicits comment on whether position visibility requirements should also be imposed on referenced agricultural contracts.

#### E. Aggregation of Accounts

Proposed § 151.7 would establish account aggregation standards specifically for positions in referenced contracts. Under the proposed standards, the Federal position limits in referenced contracts would apply to all positions in accounts in which any trader, directly or indirectly, has an ownership or equity interest of 10 percent or greater or, by power of attorney or otherwise, controls trading. These standards for aggregation are consistent with the standards delineated in the Acceptable Practice to DCM Core Principle 5 in Appendix B to part 38 of the Commission's regulations. Proposed § 151.7 would also treat positions held by two or more traders acting pursuant to an express or implied agreement or understanding the same as if the positions were held by, or the trading of the positions were done by, a single trader. Proposed § 151.7 would require a trader to aggregate positions in multiple accounts or pools, including passively managed index funds, if those accounts or pools had identical trading strategies.

Proposed § 151.7(c) establishes a limited exemption for positions in pools in which a person that is a limited partner, shareholder or similar person has an ownership or equity interest of between 10 percent and 25 percent, if the person does not have control over or knowledge of the pool's trading. Proposed § 151.7(e) establishes a limited exemption for the positions of futures commission merchants in certain discretionary accounts, if they maintain only minimum control over trading in the relevant account and if the trading decisions of that account are independent from trading decisions in the futures commission merchants'

other accounts. Finally, proposed § 151.7(f) establishes a limited exemption for entities to disaggregate the positions of an independently controlled and managed trader that is not a financial entity, defined as an owned non-financial entity, in which it has an ownership or equity interest of 10 percent or greater, and it provides a non-exhaustive description of indicia that demonstrate independent control and management to the Commission. In all three cases, the exemption would only become effective upon the Commission's approval of an application described in proposed § 151.7(g).

In the aggregation standards currently in force in part 150 of the Commission's regulations, eligible entities (a broad group that includes banks, insurance companies, mutual funds, commodity pool operators and commodity trading advisors) are permitted to disaggregate positions pursuant to a self-executing independent account controller framework. Part 150 also provides expansive disaggregation provisions for commodity pool operators, limited partners and other pool participants as well as for futures commission merchants.

These disaggregation exceptions may be incompatible with the proposed Federal position limit framework and used to circumvent its requirements. Given that the proposed framework sets high position levels that are reflective of the largest positions held by market participants, permits for the netting of positions for like referenced contracts within each applicable position limit, and includes a conditional-spot-month limit for cash-settled contracts and exemptions for *bona fide* hedging (either directly or as a result of the look-through provision), allowing traders to establish a series of positions each near a proposed position limit, without aggregation, may not be appropriate. In addition, the self-executing nature of the exemptions creates an insufficient and inefficient verification regime and ultimately diminishes the Commission's ability to properly perform its market surveillance responsibilities.

Thus, the proposed aggregation standards differ in several respects from the current standards in part 150. The proposed regulations would require aggregation for a passive pool participant with a 10 percent or greater ownership or equity interest (unless the pool operator had proper information barriers in place and the pool participant did not have control over the pool's trading decisions). By comparison, under current part 150, a passive pool participant would

aggregate its positions only if it was also a principal or affiliate of the pool operator. The proposed regulations would require aggregation for any passive pool participant with a 25 percent or greater ownership or equity interest, with no possibility for disaggregation, whereas current part 150 only follows such an approach for pools with operators that are exempt from registration under § 4.13. The proposed regulations would also require aggregation for positions in accounts or pools with identical trading strategies, which part 150 currently lacks, in order to prevent circumvention of the aggregation requirements by, for example, a trader seeking a large long-only position in a given commodity through specific positions in multiple pools.

In addition, the proposed regulations do not retain the independent account controller exemption of part 150. The regulations proposed in January of 2010 to establish position limits for referenced energy contracts also did not include an independent account controller framework; they included only a very narrow exemption thereto for certain passive pool participants.<sup>42</sup> Many commenters to the January 2010 proposed regulations expressed opposition to such strict standards, arguing that they would force aggregation of positions in situations where meaningful control, management and information barriers demonstrated sufficient independence to warrant disaggregation. The current regulations address some of these concerns by establishing a limited exemption for owned non-financial entities.

The owned non-financial entity exemption would allow an entity to disaggregate (1) the positions of a non-financial entity in which it owns a 10 percent or greater ownership or equity interest from (2) its own directly held or controlled positions and the positions attributed to it (through the general 10 percent ownership standard or other aggregation requirements of the proposed regulations), if it can demonstrate that the owned non-financial entity is independently controlled and managed. This limited exemption aims to allow disaggregation primarily in the case of a conglomerate or holding company that merely has a passive ownership interest in one or more non-financial operating companies. In such cases, the operating companies may have complete trading and management independence and operate at such a distance from the holding company that it would not be

<sup>42</sup> See 75 FR 4144, at 4146.

appropriate to aggregate positions. Two of the criteria proposed as indicia of independence are similar to those currently contained in part 150, namely the requirements that the entity have no knowledge of the owned non-financial entity's trading decisions (along with, in the proposed regulations, the reverse requirement that the owned non-financial entity have no knowledge of the entity's trading decisions) and that the owned non-financial entity have written policies and procedures to protect such knowledge. Two other proposed indicia not found in current part 150, requiring separate employees and risk management systems, would provide further evidence of the owned non-financial entity's independence. As mentioned above, the indicia described in proposed § 151.7(f) are not meant to form an exhaustive list; under the proposed application process described in 151.7(g), a departure from the self-executing exemption of part 150, the applying entity could describe for the Commission any other relevant circumstances that would warrant disaggregation.

The Commission solicits comments on all aspects of its account aggregation regulations. In particular, the Commission solicits comments on the appropriateness of the definition of owned non-financial entities and the criteria used to determine the independence of such entities. The Commission also solicits comments on whether and under what circumstances the Commission should grant exemptions from account aggregation under its exemptive authority under section 4a(a)(7) of the Act.

#### F. Preexisting Positions and Exemptions

Consistent with the good faith exemption in section 4a(b)(2) of the Act, the Commission will provide a limited exemption for positions in DCM contracts for future delivery or option contracts that are in excess of a position limit in proposed § 151.2, provided that they were established in good faith prior to the effective date of a position limit set by rule, regulation or order. Such persons would not be allowed to enter into new, additional contracts in the same direction but could take up offsetting positions and thus reduce their total combined net position.<sup>43</sup> Persons who established a net position below the speculative limit for a contract for future delivery prior to the enactment of a regulation would be permitted to acquire new positions.

<sup>43</sup> The Commission understands that changes in option deltas could increase the net level of a person's pre-enactment position.

However, consistent with Commission practice, the Commission would calculate the combined position of a person based on any position established prior to enactment of a position limit rule, regulation or order plus any new position.

In contrast to futures and option contracts, the proposed regulations would not apply position limits to Dodd-Frank Act pre-effective date swaps. The Commission is proposing this broad exemption since swaps generally may be appreciably longer lived than futures contracts thereby giving rise to concerns that position limits affecting pre-effective date swaps may unnecessarily disrupt position hedging through swap positions. The Commission would allow pre-effective date swaps to be netted with post-effective date swaps for the purpose of complying with position limits.

The Commission has previously granted certain swap dealers hedge exemptions under current § 1.47, without regard to the purposes or hedging needs of swap dealer counterparties. The Commission intends to permit such swap dealers to continue to manage the risk of a swap portfolio that exists at the time of implementation of the proposed regulations. No new swaps will be covered by the exemption.

In this regard, the Commission seeks comment on what additional reporting requirements, if any, it should impose on swap dealers that were granted a hedge exemption.

#### G. Foreign Boards of Trade

Proposed § 151.8 would provide that the aggregate position limits in proposed § 151.4 apply to a trader's positions in referenced contracts executed on, or pursuant to the rules of, a foreign board of trade, subject to the following conditions. First, the FBOT contract, agreement, or transaction must settle against the price of a contract executed or cleared pursuant to the rules of a registered entity. Second, the FBOT must make such linked contracts available to its members or other participants located in the United States by direct access to its electronic trading and order matching system.

#### H. Registered Entity Position Limits

Proposed § 151.11 requires registered entities<sup>44</sup> to establish position limits for reference contracts that are at a level no higher than the position limits specified in proposed § 151.4. Proposed

<sup>44</sup> Relevant for these purposes, CEA section 1a(40), as amended by the Dodd-Frank Act, would define registered entity to include DCMs and SEFs.

§ 151.11(c) and (d)(1)(i) would require registered entities to follow the same account aggregation and *bona fide* exemption standards set forth by proposed § 151.5 and § 151.7 with respect to exempt and agricultural commodities.

For excluded commodities,<sup>45</sup> consistent with current DCM practice, registered entities would have the discretion to establish position accountability levels in lieu of position limits. Registered entities may impose position accountability rules in lieu of position limits only if either: The open interest in a contract is less than 5,000; or the contract involves a major currency; or involves an excluded commodity that has the following three characteristics: (1) An average daily open interest of 50,000 or more contracts, (2) an average daily trading volume of 100,000 or more contracts, and (3) a highly liquid cash market.

With respect to excluded commodities, consistent with the current DCM practice, registered entities may provide for exemptions from their position limits for "*bona fide* hedging." The term "*bona fide* hedging," as used with respect to excluded commodities, shall be defined in accordance with amended CFTC § 1.3(z).<sup>46</sup> Additionally, consistent with the current DCM practice, registered entities may continue to provide exemptions for "risk-reducing" and "risk-management" transactions or positions consistent with existing Commission guidelines.<sup>47</sup> Finally, though the Commission is removing the procedure to apply to the Commission for *bona fide* hedge exemptions for non-enumerated transactions or positions under § 1.3(z)(3), the Commission will continue to recognize prior Commission determinations under that section, and registered entities may recognize non-enumerated hedge transactions subject to Commission review.

#### I. Delegation

Proposed § 151.12 delegates certain of the Commission's proposed part 151 authority to the Director of the Division of Market Oversight and to other employee or employees as designated by the Director. The delegated authority

<sup>45</sup> See section 1a(19) of the Act.

<sup>46</sup> See Section 151.11(d)(1)(ii) of these proposed regulations. As explained in section C of this release, the definition of *bona fide* hedge transaction or position contained in section 4a(c)(2) of the Act does not, by its terms, apply to excluded commodities.

<sup>47</sup> See *Clarification of Certain Aspects of Hedging Definition*, 52 FR 27195, Jul. 20, 1987; and *Risk Management Exemptions From Speculative Position Limits Approved under Commission Regulation 1.61*, 52 FR 34633, Sept. 14, 1987.

extends to: (1) Determining open interest levels for the purpose of setting non-spot-month position limits; (2) granting an exemption relating to *bona fide* hedging transactions; and (3) providing instructions or determining the format, coding structure, and electronic data transmission procedures for submitting data records and any other information required under proposed part 151. The purpose of this delegation provision is to facilitate the ability of the Commission to respond to changing market and technological conditions and thus ensure timely and accurate data reporting. In this regard, the Commission specifically requests comments on whether determinations of open interest or deliverable supply should be adopted through Commission orders.

### III. Related Matters

#### A. Cost-Benefit Analysis

Section 15(a) of the Act requires that the Commission, before promulgating a regulation under the Act or issuing an order, consider the costs and benefits of its action. By its terms, CEA section 15(a) does not require the Commission to quantify the costs and benefits of a new regulation or determine whether the benefits of the regulation outweigh its costs. Rather, CEA section 15(a) simply requires the Commission to "consider the costs and benefits" of its action.

CEA section 15(a) specifies that costs and benefits shall be evaluated in light of the following considerations: (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. Accordingly, the Commission could, in its discretion, give greater weight to any of the five considerations and could, in its discretion, determine that, notwithstanding its costs, a particular regulation was necessary or appropriate to protect the public interest or to effectuate any of the provisions or to accomplish any of the purposes of the Act.

The proposed position limits and their concomitant limitation on trading activity could impose certain general but significant costs. Overly restrictive position limits could cause unintended consequences by decreasing speculative activity and therefore liquidity in the markets for the referenced contracts, impairing the price discovery process in these markets, and encouraging the

migration of speculative activity and perhaps price discovery to markets outside of the Commission's jurisdiction. The outside spot-month position limits that would likely result from the application of the 10, 2.5 percent open interest formula, as proposed, are intended as high levels that speculators are likely to acquire in order to avoid disrupting or interfering with beneficial speculative trading.

Congress has charged the Commission with establishing position limits on traders in certain physical commodity derivatives. In CEA section 4a(a)(3), Congress directed the Commission to establish such position limits in order to achieve, to the maximum extent practicable, in the Commission's discretion, the following objectives: To diminish, eliminate, or prevent excessive speculation; to deter and prevent market manipulation; while ensuring sufficient market liquidity for *bona fide* hedgers and protecting the price discovery function of commodity derivatives. Insofar as the provisions of the proposed part 151 effectuate these goals, then the market and the public as a whole would benefit.

In section 4a of the Act, Congress determined that excessive speculation in "any commodity under contracts of sale of such commodity for future delivery \* \* \* or swaps that perform a significant price discovery function with respect to regulated entities causing sudden or unreasonable fluctuations or unwarranted changes in the price of such commodity, is an undue and unnecessary burden on interstate commerce." In section 4a(a)(3) of the Act, Congress charged the Commission with the task of setting position limits designed to diminish, eliminate, or prevent "excessive speculation." Accordingly, the speculative position limit framework established by the Commission would be expected to benefit the public and the markets regulated by the Commission by diminishing, eliminating, or preventing the undue burdens on interstate commerce that result from excessive speculation in markets regulated by the Commission.

In addition, the proposed visibility levels and associated reporting requirements of proposed § 151.6 would enable the Commission to better understand generally the portfolio compositions, including *bona fide* hedging needs, of the largest position holders of referenced contracts. This data would enable the Commission to determine whether to readjust the speculative position limits to continue to ensure the statutory objectives are met. Visibility reports would allow the

Commission to have a better sense of the relative distribution of speculative versus non-speculative positions and activity, as well as the nature and effect of the largest speculative traders in referenced contracts.

Section 4a(a)(3) of the Act also charges the Commission with setting position limits designed to "deter and prevent market manipulation." The limitation on a trader's ability to take a very large position, not justified by a *bona fide* hedging need, may reduce a trader's ability to manipulate a market. By reducing a trader's ability to manipulate a market, a position limit regime would prevent manipulation and therefore avoid the resulting price distortions, economic harm, and misallocation of resources. In addition, the visibility levels and associated reporting obligations, as proposed in § 151.6, would provide the Commission greater visibility into the portfolios of large speculative traders, thereby potentially facilitating early regulatory intervention when potential manipulative conduct or price distortions are detected.

In addition to reducing the undue burdens arising from excessive speculation and manipulation, by reducing the ability of a market participant to gain very large speculative exposure in referenced contracts, proposed part 151 would encourage better risk management, reduce the likelihood of default, and may thereby reduce systemic risk. Although futures markets employ centralized clearing arrangements that reduce systemic risk, a very large speculative position taken by a levered participant across futures markets, other trading facilities, and in over-the-counter derivatives can result in a default risk not properly accounted for by any one trading venue or counterparty. The proposed regulations may therefore promote the financial integrity of the markets and protect the public by reducing systemic risk insofar as the provisions of the proposed part 151 would reduce the likelihood of such levered entities to generate systemic risk by either limiting their ability to amass a very large speculative position or by making such entities more visible to the Commission pursuant to proposed § 151.6.

The Commission invites public comment on its cost-benefit considerations. Commenters are also invited to submit any data or other information that they may have quantifying or qualifying the costs and benefits of proposed part 151.

### B. The Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA), 5 U.S.C. 601 *et seq.*, requires that agencies consider the impact of their regulations on small businesses. The requirements related to the proposed amendments fall mainly on registered entities, exchanges, futures commission merchants, swap dealers, clearing members, foreign brokers, and large traders. The Commission has previously determined that exchanges, futures commission merchants and large traders are not “small entities” for the purposes of the RFA.<sup>48</sup> Similarly, swap dealers, clearing members, foreign brokers and traders would be subject to the proposed regulations only if carrying or holding large positions. Accordingly, the Chairman, on behalf of the Commission, hereby certifies, pursuant to 5 U.S.C 605(b), that the actions proposed to be taken herein would not have a significant economic impact on a substantial number of small entities.

### C. Paperwork Reduction Act

#### 1. Overview

The Paperwork Reduction Act (“PRA”)<sup>49</sup> imposes certain requirements on Federal agencies in connection with their conducting or sponsoring any collection of information as defined by the PRA. Certain provisions of the proposed regulations would result in new collection of information requirements within the meaning of the PRA. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid control number. The Office of Management and Budget (“OMB”) has not yet assigned a control number to the new collections associated with these proposed regulations. Therefore, the Commission is submitting this proposal to OMB for review in accordance with 44 U.S.C. 3507(d) and 5 CFR 1320.11. The title for this proposed collection of information is “Part 151—Position Limit Framework for Referenced Contracts” (OMB control number 3038–NEW).

If adopted, responses to this collection of information would be mandatory. The Commission will protect proprietary information according to the Freedom of Information Act and 17 CFR part 145, headed “Commission Records and Information.” In addition, the Commission emphasizes that section 8(a)(1) of the Act strictly prohibits the Commission, unless specifically authorized by the Act, from making public “data and

information that would separately disclose the business transactions or market positions of any person and trade secrets or names of customers.”<sup>50</sup> The Commission also is required to protect certain information contained in a government system of records pursuant to the Privacy Act of 1974.<sup>51</sup>

Under the proposed regulations, market participants with positions in referenced contracts, as defined in proposed § 151.2, would be subject to the position limit framework established by proposed part 151. Proposed part 151 prescribes reporting requirements for traders claiming compliance with the conditional spot-month position limit (proposed § 151.4(a)(2)), reporting requirements for DCMs that list a referenced contract (proposed § 151.4(c)), traders claiming a *bona fide* hedging exemption (proposed § 151.5(b) and (c)), traders claiming a *bona fide* hedge that does not involve the same quantity or commodity as the quantity or commodity associated with positions in referenced contracts that are used to hedge risk (proposed § 151.5(f)), traders claiming a *bona fide* swap counterparty exemption (proposed § 151.5(d)), traders with positions above a visibility level (proposed § 151.6(a)), and entities seeking an exemption to mandatory account aggregation regulations (proposed § 151.7(g)). In addition to these reporting requirements, proposed § 151.5(e) and (g) specify recordkeeping requirements for traders who receive *bona fide* hedge exemptions, as well as for swap counterparties for which the transaction would qualify as a *bona fide* hedging transaction.

#### 2. Information Provided and Recordkeeping Duties

Proposed § 151.4(a)(2) provides for a special conditional spot-month limit for traders under certain conditions, including the submission of a certification that the trader meets the required conditions. These certifications would be filed within a day after the trader exceeds a conditional spot-month limit.

The Commission anticipates that approximately one-hundred traders a year will submit conditional spot-month limit certifications. The Commission estimates that these one-hundred entities would incur a total burden of 2,400 annual labor hours resulting in a total of \$189,000 in annual labor costs.<sup>52</sup>

<sup>50</sup> 7 U.S.C. 12(a)(1).

<sup>51</sup> 5 U.S.C. 552a.

<sup>52</sup> The Commission staff’s estimates concerning the wage rates are based on salary information for the securities industry compiled by the Securities Industry and Financial Markets Association (“SIFMA”). The \$78.61 per hour is derived from

and \$1 million in annualized capital and start-up costs<sup>53</sup> and annual total operating and maintenance costs.

Proposed § 151.4(c) requires that DCMs submit an estimate of deliverable supply by the 31st of December of each calendar year for each referenced contract that is subject to a spot-month position limit and listed or executed pursuant to the rules of the DCM. The Commission estimates that this proposed reporting regulation will affect approximately six entities annually resulting in a total marginal burden, across all of these entities, of 6,000 annual labor hours and \$55,000 in annualized capital and start-up costs and annual total operating and maintenance costs.

Proposed § 151.5 sets forth the application procedure for *bona fide* hedgers and counterparties to *bona fide* hedging swap transactions that seek an exemption from the proposed Commission-set federal position limits for referenced contracts. If a *bona fide* hedger seeks to claim an exemption from position limits because of cash market activities, then the hedger would submit a 404 filing pursuant to proposed § 151.5(b). The 404 filing would be submitted when the *bona fide* hedger claims an exemption or when its hedging needs increase. Parties to *bona fide* hedging swap transactions would be required to submit a 404S filing to qualify for a hedging exemption, which would also be submitted when the *bona fide* hedger claims an exemption or when its hedging needs increase. If a *bona fide* hedger seeks an exemption for anticipated commercial production or anticipatory commercial requirements, then the hedger would submit a 404A filing pursuant to proposed § 151.5(c). The 404A filing would be submitted at least ten days in advance of the date that transactions and positions would be established that would exceed a position limit. Further, on an annual basis or whenever a trader’s anticipated hedge requirements exceed the amount of the most recent 404A filing,

figures from a weighted average of salaries and bonuses across different professions from the SIFMA Report on Management & Professional Earnings in the Securities Industry 2010, modified to account for an 1800-hour work-year and multiplied by 1.3 to account for overhead and other benefits. The wage rate is a weighted national average of salary and bonuses for professionals with the following titles (and their relative weight): “programmer (senior)” (30% weight); “programmer” (30%); “compliance advisor (intermediate);” (20%), “systems analyst;” (10%); and “assistant/associate general counsel” (10%).

<sup>53</sup> The capital/start-up cost component of “annualized capital/start-up, operating, and maintenance costs” is based on an initial capital/start-up cost that is straight-line depreciated over five years.

<sup>48</sup> 44 U.S.C. 601 *et seq.*

<sup>49</sup> 44 U.S.C. 3501 *et seq.*

whichever is earlier, the trader would be required to file a supplemental report updating the information provided in the most recent 404A filing. Traders hedging commercial activity (or hedging swaps that in turn hedge commercial activity) that does not involve the same quantity or commodity as the quantity or commodity associated with positions in referenced contracts that are used to hedge shall submit the conversion methodology and information along with the appropriate 404, 404A, or 404S filing. The Commission anticipates that the compliance cost associated with all of these filings will be substantial, particularly in the case of the 404S filings, which may require the collection and storage of information on counterparties that firms have hitherto not conducted.

The Commission estimates that these bona fide hedging-related reporting requirements would affect approximately two hundred entities annually and result in a total burden of approximately \$37.6 million across all of these entities, of 168,000 annual labor hours resulting in a total of \$13.2 million in annual labor costs and \$25.4 million in annualized capital and start-up costs and annual total operating and maintenance costs. 404 filings proposed reporting regulations would affect approximately ninety entities annually resulting in a total burden, across all of these entities, of 108,000 total annual labor hours and \$11.7 million in annualized capital and start-up costs and annual total operating and maintenance costs. 404A filings proposed reporting regulations would affect approximately sixty entities annually resulting in a total burden, across all of these entities, of 6,000 total annual labor hours and \$4.2 million in annualized capital and start-up costs and annual total operating and maintenance costs. 404S filings proposed reporting regulations would affect approximately forty-five entities annually resulting in a total burden, across all of these entities, of 54,000 total annual labor hours and \$9.5 million in annualized capital and start-up costs and annual total operating and maintenance costs.

Proposed § 151.5(e) specifies recordkeeping requirements for traders who claim bona fide hedge exemptions. These recordkeeping requirements include "complete books and records concerning all of their related cash, futures, and swap positions and transactions and make such books and records, along with a list of swap counterparties." Proposed § 151.5(g) and (h) provide procedural documentation requirements for those availing

themselves of a bona fide hedging transaction exemption. These firms would be required to document a representation and confirmation by at least one party that the swap counterparty is relying on a bona fide hedge exemption, along with a confirmation of receipt by the other party to the swap. Paragraph (h) of Section 151.5 also requires that the written representation and confirmation be retained by the parties and available to the Commission upon request. The marginal impact of this requirement is limited because of its overlap with existing recordkeeping requirements under § 15.03. The Commission estimates that bona fide hedging-related proposed recordkeeping regulations would affect approximately one-hundred and sixty entities resulting in a total burden, across all of these entities, of 40,000 total annual labor hours and \$10.4 million in annualized capital and start-up costs and annual total operating and maintenance costs.

Proposed § 151.6 would require those traders with positions exceeding visibility levels in referenced base and precious metals and energy commodities to submit additional information about cash market and derivatives activity in substantially the same commodity. Proposed § 151.6(b) would require the submission of a 401 filing which would provide basic position information on the position exceeding the visibility level. Proposed § 151.6(c) would require additional information, through a 402S filing, on a trader's uncleared swaps in substantially the same commodity. Proposed § 151.6(d) would require the reportable trader to submit information about cash market positions or anticipated commercial requirements or production in substantially the same commodity, as described in proposed § 151.5(b) and (c), through a 404 or 404A filing, respectively. All of the proposed 151.6 reports would be submitted on a monthly basis for as long as a trader exceeds a visibility level.

The Commission estimates that visibility level-related proposed reporting regulations will affect approximately one-hundred and forty entities annually resulting in a total burden, across all of these entities, of 30,400 annual labor hours resulting in a total of \$2.4 million in annual labor costs and \$27.3 million in annualized capital and start-up costs and annual total operating and maintenance costs. Proposed 401 filing reporting regulations would affect approximately one-hundred and forty entities annually resulting in a total burden, across all of these entities, of 168,000 total annual

labor hours and \$15.4 million in annualized capital and start-up costs and annual total operating and maintenance costs. Proposed 402S filing reporting regulations would affect approximately seventy entities annually resulting in a total burden, across all of these entities, of 5,600 total annual labor hours and \$4.9 million in annualized capital and start-up costs and annual total operating and maintenance costs. Proposed visibility level-related 404 filing reporting regulations<sup>54</sup> would affect approximately sixty entities annually resulting in a total burden, across all of these entities, of 4,800 total annual labor hours and \$4.2 million in annualized capital and start-up costs and annual total operating and maintenance costs. Proposed visibility level-related 404A filing reporting regulations would affect approximately forty entities annually resulting in a total burden, across all of these entities, of 3,200 total annual labor hours and \$2.8 million in annualized capital and start-up costs and annual total operating and maintenance costs.

Proposed § 151.7 concerns the aggregation of trader accounts. Proposed § 151.7(g) would provide for a disaggregation exemption for: (1) A limited partner, shareholder or similar person with an ownership or equity interest of between 10 percent and 25 percent in a pool, if the trader does not have control over or knowledge of a pool's trading; (2) futures commission merchants that meet certain independent trading requirements; and (3) an independently controlled and managed trader, that is not a financial entity, in which another entity has an ownership or equity interest of 10 percent or greater. In all three cases, the exemption would become effective upon the Commission's approval of an application described in proposed § 151.7(g). These applications for exemptions would be submitted at the time a trader claims an exemption and within thirty calendar days of January 1 of each year following the initial application for exemption. The Commission estimates that these proposed reporting regulations will affect approximately sixty entities resulting in a total burden, across all of these entities, of 300,000 annual labor

<sup>54</sup> For the visibility level-related 404 and 404A filing requirements, the estimated burden is based on reporting duties not already accounted for in the burden estimate for those submitting 404 or 404A filings pursuant to proposed regulation 151.5. For many of these firms, the experience and infrastructure developed submitting or preparing to submit a 404 or 404A filing under proposed regulation 151.5 would reduce the marginal burden imposed by having to submit filings under proposed regulation 151.6.

hours and \$9.9 million in annualized capital and start-up costs and annual total operating and maintenance costs.

### 3. Comments on Information Collection

The Commission invites the public and other federal agencies to comment on any aspect of the reporting and recordkeeping burdens discussed above. Pursuant to 44 U.S.C. 3506(c)(2)(B), the Commission solicits comments in order to: (1) Evaluate whether the proposed collections of information are necessary for the proper performance of the functions of the Commission, including whether the information will have practical utility; (2) evaluate the accuracy of the Commission's estimate of the burden of the proposed collections of information; (3) determine whether there are ways to enhance the quality, utility, and clarity of the information to be collected; and (4) minimize the burden of the collections of information on those who are to respond, including through the use of automated collection techniques or other forms of information technology.

Comments may be submitted directly to the Office of Information and Regulatory Affairs, by fax at (202) 395-6566 or by e-mail at [OIRA-submissions@omb.eop.gov](mailto:OIRA-submissions@omb.eop.gov). Please provide the Commission with a copy of comments submitted so that all comments can be summarized and addressed in the final regulation preamble. Refer to the Addresses section of this notice for comment submission instructions to the Commission. A copy of the supporting statements for the collection of information discussed above may be obtained by visiting [RegInfo.gov](http://RegInfo.gov). OMB is required to make a decision concerning the collection of information between 30 and 60 days after publication of this release. Consequently, a comment to OMB is most assured of being fully considered if received by OMB (and the Commission) within 30 days after the publication of this notice of proposed rulemaking.

#### List of Subjects

##### 17 CFR Part 1

Brokers, Commodity futures, Consumer protection, Reporting and recordkeeping requirements.

##### 17 CFR Part 150

Commodity futures, Cotton, Grains.

##### 17 CFR Part 151

Position limits, Bona fide hedging, Referenced contracts.

In consideration of the foregoing, pursuant to the authority contained in

the Commodity Exchange Act, the Commission hereby proposes to amend chapter I of title 17 of the Code of Federal Regulations as follows:

### PART 1—GENERAL REGULATIONS UNDER THE COMMODITY EXCHANGE ACT

1. The authority citation for part 1 is revised to read as follows:

**Authority:** 7 U.S.C. 1a, 2, 5, 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, and 24, as amended by Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, 124 Stat. 1376 (2010).

2. Amend § 1.3(z) as follows:

a. Amend the heading in paragraph (z) by adding “for excluded commodities” after the phrase “positions.”

b. Amend paragraph (z)(1) introductory text by removing the phrase “transactions or positions in a contract for future delivery on any contract market, or in a commodity option” after the phrase “Bona fide hedging transactions or positions shall mean,” and by adding, in its place, the phrase “any agreement, contract or transaction in an excluded commodity on a registered entity, as that term is defined in Section 1a(40) of the Act.”

c. Amend paragraph (z)(1) concluding text by removing “and §§ 1.47 and 1.48 of the regulations.”

d. Amend paragraph (z)(2)(i) by removing the phrase “commodity for future delivery on a contract market” after “Sales of any” and by adding, in its place, the phrase “agreement, contract or transaction in a excluded commodity on a registered entity.”

e. Amend paragraph (z)(2)(i)(B) by removing the phrase “future during the five last trading days of that future” and by adding, in its place, the phrase “agreement, contract or transaction during the five last trading days.”

f. Amend paragraph (z)(2)(ii) by removing the phrase “commodity for future delivery on a contract market” after “Purchases of any” and by adding, in its place, the phrase “agreement, contract or transaction in a excluded commodity on a registered entity.”

g. Amend paragraph (z)(2)(ii)(C) by removing the phrase “one future” and by adding, in its place, the phrase “agreement, contract or transaction.”

h. Amend paragraph (z)(2)(iii) by removing the phrase “for future delivery on a contract market” after “Offsetting sales and purchases” and by adding, in its place, the phrase “in any agreement, contract or transaction in a excluded commodity on a registered entity.”

i. Amend paragraph (z)(2)(iii) by removing the phrase “future during the

five last trading days of that future” and by adding, in its place, the phrase “agreement, contract or transaction during the five last trading days.”

j. Redesignate paragraph (z)(2)(iv) as paragraph (z)(2)(v).

k. Amend newly redesignated paragraph (z)(2)(v) by removing the phrase “for future delivery described in paragraphs (z)(2)(i), (z)(2)(ii) and (z)(2)(iii)” and by adding, in its place, the phrase “described in paragraphs (z)(2)(i), (z)(2)(ii), (z)(2)(iii) and (z)(2)(iv).”

l. Amend newly redesignated paragraph (z)(2)(v) by removing the phrase “for future delivery” after the phrase “fluctuations in value of the position” and by adding, in its place, the phrase “in any agreement, contract or transaction.”

m. Amend newly redesignated paragraph (z)(2)(v) by removing the phrase “positions in any one future shall not be maintained during the five last trading days of that future” and by adding, in its place, the phrase “positions in any agreement, contract or transaction shall not be maintained during the five last trading days.”

n. Add new paragraph (z)(2)(iv) and revise paragraph (z)(3) to read as follows:

#### § 1.3 Definitions.

\* \* \* \* \*

(z) \* \* \*

(2) \* \* \*

(iv) Purchases or sales by an agent who does not own or has not contracted to sell or purchase the offsetting cash commodity at a fixed price, provided that the person is responsible for the merchandising of the cash positions which is being offset and the agent has a contractual arrangement with the person who owns the commodity or holds the cash market commitment being offset.

\* \* \* \* \*

(z)(3) *Non-Enumerated cases.* A registered entity may recognize, consistent with the purposes of this section, transactions and positions other than those enumerated in paragraph (2) of this section as bona fide hedging. Prior to recognizing such non-enumerated transactions and positions, the registered entity shall submit such rules for Commission review under section 5c of the Act and § 40 of this chapter.

\* \* \* \* \*

#### § 1.47 [Removed and Reserved]

3. Remove and reserve § 1.47.

#### § 1.48 [Removed and Reserved]

4. Remove and reserve § 1.48.



**PART 150—[REMOVED AND RESERVED]**

5. Remove and reserve part 150.
6. Add part 151 to read as follows:

**PART 151—LIMITS ON POSITIONS**

## Sec.

- 151.1 Definitions.
- 151.2 Core referenced futures contracts.
- 151.3 Referenced contract spot months.
- 151.4 Position limits for referenced contracts.
- 151.5 Exemptions for referenced contracts.
- 151.6 Position visibility.
- 151.7 Aggregation of positions.
- 151.8 Foreign boards of trade.
- 151.9 Preexisting positions.
- 151.10 Form and manner of reporting and submitting information or filings.
- 151.11 Registered entity position limits.
- 151.12 Delegation of authority to the Director of the Division of Market Oversight.

## Appendix A to Part 151

**Authority:** 7 U.S.C. 1a, 2, 5, 6, 6a, 6c, 6f, 6g, 6t, 12a, 19, as amended by Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, 124 Stat. 1376 (2010).

**§ 151.1 Definitions.**

As used in this part—

*Basis contract* means an agreement, contract or transaction that is cash settled based on the difference in price of the same commodity (or substantially the same commodity) at different delivery points;

*Calendar spread contract* means a cash settled agreement, contract or transaction that represents the difference between the settlement price in one or a series of contract months of an agreement, contract or transaction and another contract month's or another series of contract months' settlement price for the same agreement, contract or transaction.

*Contracts of the same class* mean referenced contracts based on the same commodity that are:

- (1) Futures or option contracts executed pursuant to the rules of a designated contract market; or
- (2) Cleared or uncleared swaps.

*Commodity index contract* means an agreement, contract or transaction that is not a basis or spread contract, based on an index comprised of prices of commodities that are not the same nor substantially the same, *provided that*, a commodity index contract that incorporates the price of a commodity underlying a referenced contract's commodity which is used to circumvent speculative position limits shall be considered to be a referenced contract for the purpose of applying the position limits of § 151.4.

*Core referenced futures contract* means a futures contract that is listed in § 151.2.

*Entity* means a "person" as defined in section 1a of the Act.

*Excluded commodity* means an "excluded commodity" as defined in section 1a of the Act.

*Financial entity* means any entity that, regardless of any asset or capital threshold or any other condition in section 1a(18) of the Act, is an entity identified in section 1a(18)(A)(i) through (iv), (vi), (viii) through (x) and (B)(ii) of the Act.

*Futures contract class* means referenced contracts that are based on the same commodity and are futures and option contracts executed pursuant to the rules of a designated contract market.

*Intercommodity spread contract* means a cash-settled agreement, contract or transaction that represents the difference between the settlement price of a referenced contract and the settlement price of another contract, agreement, or transaction that is based on a different commodity.

*Owned non-financial entity* means any entity that is not a financial entity and in which another entity directly or indirectly has a 10 percent or greater ownership or equity interest.

*Referenced contract* means, on a futures equivalent basis with respect to a particular core referenced futures contract, a futures listed in § 151.2, or a referenced paired futures contract, option contract, swap or swaption, other than a basis contract or contract on a commodity index.

*Referenced paired futures contract, option contract, swap or swaption* means, respectively, an open futures contract, option contract, swap or swaption that is:

- (1) Directly or indirectly linked, including being partially or fully settled on, or priced at a differential to, the price of any core referenced futures contract; or
- (2) Directly or indirectly linked, including being partially or fully settled on, or priced at a differential to, the price of the same commodity for delivery at the same location, or at locations with substantially the same supply and demand fundamentals, as that of any core referenced futures contract.

*Spot month* means, for referenced contracts based on a commodity identified in § 151.3, the spot month corresponding to the spot month of the core futures contract that overlies the same commodity.

*Spot-month, single-month, and all-months-combined position limits* mean,

for referenced contracts based on a commodity identified in § 151.3, the position limit corresponding to the position limit of the core futures contract that overlies the same commodity.

*Spread contract* means either a calendar spread contract or an intercommodity spread contract.

*Swap* means "swap" as defined in section 1a of the Act and as further defined by the Commission.

*Swap contract class* means referenced contracts that are based on the same commodity and are swaps.

*Swaption* means an option to enter into a swap or a physical commodity option.

*Swap dealer* means "swap dealer" as that term is defined in section 1a of the Act and as further defined by the Commission.

*Trader* means a person that, for its own account or for an account that it controls, makes transactions in referenced contracts or has such transactions made.

**§ 151.2 Core referenced futures contracts.**

(a) *Agricultural commodities.* The core referenced futures contracts include:

(1) *ICE Futures U.S. Cocoa* (CC) contract based on a trading unit of 10 metric tons delivered at licensed warehouses in the Port of New York District, Delaware River Port District, Port of Hampton Roads, Port of Albany, or Port of Baltimore;

(2) *ICE Futures U.S. Coffee C* (KC) contract based on a trading unit of 37,500 pounds delivered at the Port of New York District, the Port of New Orleans, the Port of Houston, the Port of Bremen/Hamburg, the Port of Antwerp, the Port of Miami, or the Port of Barcelona;

(3) *Chicago Board of Trade Corn* (C) contract based on a trading unit of 5,000 bushels delivered at Chicago and Burns Harbor, Indiana Switching District, Lockport-Seneca Shipping District, Ottawa-Chillicothe Shipping District, or Peoria-Pekin Shipping District;

(4) *ICE Futures U.S. Cotton No. 2* (CT) contract based on a trading unit of 50,000 pounds net weight delivered at Galveston, Texas; Houston, Texas; New Orleans, Louisiana; Memphis, Tennessee; or Greenville/Spartanburg, South Carolina;

(5) *Chicago Mercantile Exchange Feeder Cattle* (FC) contract based on a trading unit of 50,000 pounds priced based on the CME Feeder Cattle Index or any other contract based on a sample of feeder cattle sales transactions in Colorado, Iowa, Kansas, Missouri, Montana, Nebraska, New Mexico, North

Dakota, Oklahoma, South Dakota, Texas, and Wyoming;

(6) *ICE Futures U.S. FCOJ-A* (OJ) contract based on a trading unit of 15,000 pounds delivered at licensed warehouses in Florida, New Jersey, and Delaware;

(7) *Chicago Mercantile Exchange Lean Hog* (LH) contract based on a trading unit of 40,000 pounds priced based on the CME Lean Hog Index;

(8) *Chicago Mercantile Exchange Live Cattle* (LC) contract based on a trading unit of 40,000 pounds delivered at livestock yards in Wray, Colorado, Worthing, South Dakota; Syracuse, Kansas; Tulia, Texas; Columbus, Nebraska; Dodge City, Kansas; Amarillo, Texas; Norfolk, Nebraska; North Platte, Nebraska; Ogallala, Nebraska; Pratt, Kansas; Texhoma, Oklahoma; or Clovis, New Mexico;

(9) *Chicago Mercantile Exchange Class III Milk* (DA) contract based on a trading unit of 200,000 pounds priced based on the USDA Class III price for milk;

(10) *Chicago Board of Trade Oats* (O) contract based on a trading unit of 5,000 bushels delivered at Chicago Switching District, the Burns Harbor, Indiana Switching District, Minneapolis, St. Paul, Minnesota Switching Districts, Duluth Minnesota, or Superior, Wisconsin;

(11) *Chicago Board of Trade Rough Rice* (RR) contract based on a trading unit of 200,000 pounds delivered at warehouses in the Arkansas counties of Craighead, Jackson, Poinsett, Woodruff, Cross, St. Francis, Lonoke, Prairie, Monroe, Jefferson, Arkansas, or DeSha;

(12) *Chicago Board of Trade Soybeans* (S) contract based on a trading unit of 5,000 bushels delivered at Chicago and Burns Harbor, Indiana Switching District, Lockport-Seneca Shipping District, Ottawa-Chillicothe Shipping District, Peoria-Pekin Shipping District, Havana-Grafton Shipping District, or St. Louis-East St. Louis and Alton Switching Districts;

(13) *Chicago Board of Trade Soybean Meal* (SM) contract based on a trading unit of 100 short tons shipped from plants located in the Central Territory, Northeast Territory, Mid South Territory, Missouri Territory, Eastern Iowa Territory, or Northern Territory;

(14) *Chicago Board of Trade Soybean Oil* (BO) contract based on a trading unit of 60,000 pounds delivered at warehouses located in the Illinois Territory, Eastern Territory, Eastern Iowa Territory, Southwest Territory, Western Territory or Northern Territory;

(15) *ICE Futures U.S. Sugar No. 11* (SB) contract based on a trading unit of 112,000 pounds delivered at a port in

the country of origin or in the case of landlocked countries, at a berth or anchorage in the customary port of export for the countries of Argentina, Australia, Barbados, Belize, Brazil, Colombia, Costa Rica, Dominican Republic, El Salvador, Ecuador, Fiji Islands, French Antilles, Guatemala, Honduras, India, Jamaica, Malawi, Mauritius, Mexico, Mozambique, Nicaragua, Peru, Republic of the Philippines, South Africa, Swaziland, Taiwan, Thailand, Trinidad, United States, and Zimbabwe;

(16) *ICE Futures U.S. Sugar No. 16* (SF) contract based on a trading unit of 112,000 pounds delivered at New York, Baltimore, Galveston, New Orleans, or Savannah;

(17) *Chicago Board of Trade Wheat* (W) contract based on a trading unit of 5,000 bushels delivered at Chicago Switching District, the Burns Harbor, Indiana Switching District, the Northwest Ohio Territory, on Ohio River, on Mississippi River or the Toledo, Ohio Switching District, or the St. Louis-East St. Louis and Alton Switching Districts;

(18) *Minneapolis Grain Exchange Hard Red Spring Wheat* (MWE) contract based on a trading unit of 5,000 bushels delivered at elevators located in Minneapolis/St. Paul, Red Wing, Duluth/Superior, Minnesota;

(19) *Kansas City Board of Trade Hard Winter Wheat* (KW) contract based on a trading unit of 5,000 bushels delivered at elevators in Kansas City, Missouri/Kansas; Hutchinson, Kansas; Salina/Abilene, Kansas; or Wichita, Kansas.

(b) *Metals*. The core referenced futures contracts include:

(1) *Commodity Exchange, Inc. Gold* (GC) contract based on a trading unit of 100 troy ounces delivered at Exchange-licensed warehouses;

(2) *Commodity Exchange, Inc. Silver* (SI) contract based on a trading unit of 5,000 troy ounces delivered at Exchange-licensed warehouses;

(3) *Commodity Exchange, Inc. Copper* (HG) contract based on a trading unit of 25,000 pounds delivered at licensed warehouses;

(4) *New York Mercantile Exchange Palladium* (PA) contract based on a trading unit of 100 troy ounces delivered at licensed warehouses; and

(5) *New York Mercantile Exchange Platinum* (PL) contract based on a trading unit of 50 troy ounces pounds delivered at licensed warehouses.

(c) *Energy commodities*. The core referenced futures contracts include:

(1) *New York Mercantile Exchange Light Sweet Crude Oil* (CL) contract based on a trading unit of 1,000 U.S. barrels (42,000 gallons) delivered at the

Cushing crude oil storage complex in Cushing, Oklahoma;

(2) *New York Mercantile Exchange New York Harbor No. 2 Heating Oil* (HO) contract based on a trading unit of 1,000 U.S. barrels (42,000 gallons) delivered at an ex-shore facility in New York Harbor;

(3) *New York Mercantile Exchange New York Harbor Gasoline Blendstock* (RB) contract based on a trading unit of 1,000 U.S. barrels (42,000 gallons) delivered at an ex-shore facility in New York Harbor; and

(4) *New York Mercantile Exchange Henry Hub Natural Gas* (NG) contract based on a trading unit of 10,000 million British thermal units (mmBtu) delivered at the Henry Hub pipeline interchange in Erath, Louisiana.

### § 151.3 Referenced contract spot months.

(a) *Agricultural commodities*. For referenced contracts based on agricultural commodities, the spot month shall be the period of time commencing:

(1) At the close of business on the business day prior to the first notice day for any delivery month and terminating at the end of the delivery month for the following contracts:

(i) *ICE Futures U.S. Cocoa* (CC) contract;

(ii) *ICE Futures U.S. Coffee C* (KC) contract;

(iii) *ICE Futures U.S. Cotton No. 2* (CT) contract;

(iv) *ICE Futures U.S. FCOJ-A* (OJ) contract;

(2) At the close of business three business days prior to the first trading day in the delivery month and terminating at the end of the delivery month for the following contracts:

(i) *Chicago Board of Trade Corn* (C) contract;

(ii) *Chicago Board of Trade Oats* (O) contract;

(iii) *Chicago Board of Trade Rough Rice* (RR) contract;

(iv) *Chicago Board of Trade Soybeans* (S) contract;

(v) *Chicago Board of Trade Soybean Meal* (SM) contract;

(vi) *Chicago Board of Trade Soybean Oil* (BO) contract;

(vii) *Chicago Board of Trade Wheat* (W) contract;

(viii) *Minneapolis Grain Exchange Hard Red Spring Wheat* (MW) contract;

(ix) *Kansas City Board of Trade Hard Winter Wheat* (KW) contract;

(3) At the close of business two business days after the fifteenth calendar day of the contract month or the first business day after the fifteenth should the fifteenth day be a non-business day and terminating at the end

of the delivery month for the following contracts:

(i) *ICE Futures U.S. Sugar No. 11* (SB) contract;

(ii) *ICE Futures U.S. Sugar No. 16* (SF) contract;

(4) At the close of business on the business day immediately preceding the last five business days of the contract month and terminating at the end of the delivery month for the *Chicago Mercantile Exchange Live Cattle* (LC) contract;

(5) At the close of business on the eleventh day prior to the last trading day and terminating on the last day of trading for the contract month for the following contracts:

(i) *Chicago Mercantile Exchange Feeder Cattle* (FC) contract;

(ii) *Chicago Mercantile Exchange Class III Milk* (DA) contract;

(6) At the period commencing at the close of business on the fifth day prior to the last trading day and terminating at the end of the delivery month for the *Chicago Mercantile Exchange Lean Hog* (LH) contract.

(b) *Metals*. The spot month shall be the period of time commencing at the close of business on the business day prior to the first notice day for any delivery month and terminating at the end of the delivery month for the following contracts:

(1) *Commodity Exchange, Inc. Gold* (GC) contract; and

(2) *Commodity Exchange, Inc. Silver* (SI) contract.

(3) *Commodity Exchange, Inc. Copper* (HG) contract;

(4) *New York Mercantile Exchange Palladium* (PA) contract; and

(5) *New York Mercantile Exchange Platinum* (PL) contract.

(c) *Energy commodities*. The spot month shall be the period of time commencing at the close of business three business days prior to the last day of trading in the underlying referenced futures contract and terminating at the end of the delivery period for the following contracts:

(1) *New York Mercantile Exchange Light Sweet Crude Oil* (CL) contract;

(2) *New York Mercantile Exchange New York Harbor No. 2 Heating Oil* (HO) contract;

(3) *New York Mercantile Exchange New York Harbor Gasoline Blendstock* (RB) contract; and

(4) *New York Mercantile Exchange Henry Hub Natural Gas* (NG) contract.

**§ 151.4 Position limits for referenced contracts.**

(a) *Spot-month position limits*. Except as provided in paragraph (h) of this section for initial spot-month position

limits, or as otherwise authorized by § 151.5, no trader may hold or control positions, separately or in combination, net long or net short, in referenced contracts in the same commodity when such positions are in excess of:

(1) For physical delivery referenced contracts, a *spot-month position limit* that shall be one-quarter of the estimated spot-month deliverable supply for a core referenced futures contract in the same commodity as fixed by the Commission pursuant to paragraph (c) of this section; or

(2) For cash-settled referenced contracts, a *spot-month position limit*, equal to the level fixed by paragraph (a)(1) of this section, or a *conditional-spot-month position limit*, that is five times the spot-month position limit fixed by paragraph (a)(1) of this section, *provided that the trader:*

(i) For cash-settled contracts in the spot month, shall not hold or control positions exceeding the level of any single month position limit;

(ii) Does not hold or control positions in the physical delivery referenced contract based on the same commodity that is in such contract's spot month;

(iii) Does not hold or control cash or forward positions in the referenced contract's spot month in an amount that is greater than one-quarter of the deliverable supply in the referenced contract's underlying commodity deliverable at the location or locations specified in the core referenced futures contract in the same commodity; and

(iv) Has submitted a certification to the Commission, in the form and manner provided for in § 151.10, that the trader meets the conditions of paragraphs (a)(2)(ii) and (iii) of this section.

(b) *Limited application of spot-month position limits*. Spot-month position limits shall only apply to positions in physical delivery or cash settled referenced contracts with delivery locations that match the delivery locations of a core referenced futures contracts in the same commodity.

(c) *Deliverable supply*.

(1) For the purpose of applying the spot-month position limit or conditional spot-month-position limit in paragraph (a) of this section, the Commission shall set the levels of deliverable supply in accordance with the procedure in paragraph (h) of this section.

(2) Each designated contract market shall submit to the Commission an estimate of deliverable supply by the 31st of December of each calendar year for each physical delivery referenced contract that is subject to a spot-month position limit and listed or executed

pursuant to the rules of the designated contract market.

(3) The estimate submitted under paragraph (c)(2) of this section shall be accompanied by a description of the methodology used to derive the estimate along with any statistical data supporting the designated contract market's estimate of deliverable supply.

(4) In fixing spot-month position limits under paragraph (a)(1) of this section, the Commission shall rely on the estimate provided under paragraph (c)(2) of this section unless the Commission determines to rely on its own estimate of deliverable supply.

(d) *Non-spot position limits*. Except as otherwise authorized in § 151.5, no person may hold or control positions, separately or in combination, net long or net short, in referenced contracts in the same commodity when such positions, in all months combined (including the spot month) or in a single month, are in excess of:

(1) *An all-months-combined aggregate and single-month position limits*, fixed by the Commission at 10 percent of the first 25,000 contracts of average all-months-combined aggregated open interest, as calculated by the Commission pursuant to paragraph (e) of this section, with a marginal increase of 2.5 percent thereafter;

(2) *A class all-months-combined and single-month position limit*, fixed by the Commission, for referenced contracts that are contracts of the same class, at a level equal to the all-months-combined aggregate position limit.

(3) *Legacy position limits*. Except as otherwise authorized by § 151.5, no trader may hold or control positions, separately or in combination, net long or net short, in referenced contracts in the same commodity for the commodities enumerated below, when such positions, in all-months-combined or in a single-month, are in excess of the following position limits:

Referenced contract	Position limits
Chicago Board of Trade Corn (C) contract .....	22,000
Chicago Board of Trade Oats (O) contract .....	2,000
Chicago Board of Trade Soy- beans (S) contract .....	10,000
Chicago Board of Trade Wheat (W) contract .....	6,500
Chicago Board of Trade Soy- bean Oil (BO) contract .....	6,500
Chicago Board of Trade Soy- bean Meal (SM) contract ..	6,500
Minneapolis Grain Exchange Hard Red Spring Wheat (MW) contract .....	6,500
ICE Futures U.S. Cotton No. 2 (CT) contract .....	5,000

Referenced contract	Position limits
Kansas City Board of Trade Hard Winter Wheat (KW) contract .....	6,500

(e) *Aggregated open interest calculations.* For the purpose of determining the speculative position limits in paragraph (d) of this section and in accordance with the procedure in paragraph (h) the Commission shall determine:

(1) For determining aggregate and class all-month-combined and single-month position limits under paragraph (d) of this section, the average all-months-combined aggregate open interest, is the sum for a calendar year of values obtained under paragraphs (e)(2) and (e)(3) of this section, then divided by 12, for the twelve months prior to the effective date.

(2) *The all-months futures open interest* is, at month end, the sum of all of a referenced contract's all-months-combined open futures and option contract (on a delta adjusted basis) open interests across all designated contract markets;

(3) *The all-months swaps open interest*, at month end, the sum of all of a referenced contract's all-months-combined open swaps and swaptions open interest, combining, open interest attributed to cleared and uncleared swaps and swaptions, where the uncleared all-months-combined swap open interest shall be the absolute sum of all swap dealers' net uncleared open swaps and swaptions exposures by counterparty and by single referenced contract month.

(f) *Netting of positions.* (1) For referenced contracts in the spot month, a trader's positions in physical delivery and cash-settled contracts are calculated separately and traders can have up to the spot-month position limit in both the physically delivered and cash settled contracts unless the cash settled contract positions are held pursuant to the conditional-spot-month position limit.

(2) For the purpose of applying non-spot-month position limits, a trader's position shall be combined and the net resulting position shall be applied towards determining the trader's aggregate single-month and all-months-combined position.

(3) For the purpose of applying non-spot-month class limits, a trader's position in contracts of the same class shall be combined and the net resulting position shall be applied towards determining the trader's class single-month and all-months-combined position.

(g) *Additional provisions.* In determining or calculating all levels and limits under this section, a resulting number shall be rounded up to the nearest hundred contracts.

(h) *Process for fixing and publishing position limits.* (1) With the exception of initial position limits, the Commission shall fix position limits under this part by January 31st of each calendar year;

(2) The initial spot-month position limits for referenced contracts shall be as provided in Appendix A to this part.

(3) The initial spot-month, single-month and all-months-combined position limits must be made effective pursuant to a Commission order and may be made on any date.

(4) The Commission shall publish position limits on the Commission's Web site at <http://www.cftc.gov> prior to making such limits effective, and such limits, other than initial limits, shall become effective on the 1st day of March immediately following the fixing date and shall remain effective up until and including the last day of the immediately following February.

#### **§ 151.5 Exemptions for referenced contracts.**

(a) *Bona fide hedging transactions or positions.*

(1) Any trader that complies with the requirements of this section may exceed the position limits set forth in § 151.4 to the extent that a transaction or position in a referenced contract:

(i) Represents a substitute for transactions made or to be made or positions taken or to be taken at a later time in a physical marketing channel;

(ii) Is economically appropriate to the reduction of risks in the conduct and management of a commercial enterprise; and

(iii) Arises from the potential change in the value of—

(A) Assets that a person owns, produces, manufactures, processes, or merchandises or anticipates owning, producing, manufacturing, processing, or merchandising;

(B) Liabilities that a person owns or anticipates incurring; or

(C) Services that a person provides or purchases, or anticipates providing or purchasing; or

(iv) Reduces risks attendant to a position resulting from a swap that—

(A) Was executed opposite a counterparty for which the transaction would qualify as a *bona fide* hedging transaction pursuant to paragraph (a)(1)(i) through (a)(1)(iii) of this section; or

(B) Meets the requirements of paragraphs (a)(1)(i) through (a)(1)(iii) of this section. Notwithstanding the

foregoing, no transactions or positions shall be classified as *bona fide* hedging for purposes of § 151.4 unless such transactions or positions are established and liquidated in an orderly manner in accordance with sound commercial practices and the provisions of paragraph (a)(2) of this section have been satisfied.

(2) *Enumerated Hedging Transactions.* The definition of *bona fide* hedging transactions and positions in paragraph (a)(1) of this section includes the following specific transactions and positions:

(i) Sales of any commodity underlying referenced contracts which do not exceed in quantity:

(A) Ownership or fixed-price purchase of the contract's underlying cash commodity by the same person; or

(B) Unsold anticipated production of the same commodity, which may not exceed one year for referenced agricultural contracts, by the same person provided that no such position is maintained in any referenced contract during the five last trading days of that referenced contract.

(ii) Purchases of referenced contracts which do not exceed in quantity:

(A) The fixed-price sale of the contract's underlying cash commodity by the same person;

(B) The quantity equivalent of fixed-price sales of the cash products and by-products of such commodity by the same person; or

(C) Unfilled anticipated requirements of the same cash commodity, which may not exceed one year for referenced agricultural contracts, for processing, manufacturing, or feeding by the same person, provided that such transactions and positions in the five last trading days of any referenced contract do not exceed the person's unfilled anticipated requirements of the same cash commodity for that month and the next succeeding month.

(iii) Offsetting sales and purchases in referenced contracts which do not exceed in quantity that amount of the same cash commodity which has been bought and sold by the same person at unfixed prices basis different delivery months of the referenced contract, *provided that* no such position is maintained during the five last trading days of any referenced contract.

(iv) Purchases or sales by an agent who does not own or has not contracted to sell or purchase the offsetting cash commodity at a fixed price, *provided that* the person is responsible for the merchandising of the cash positions which is being offset and the agent has a contractual arrangement with the person who owns the commodity or

holds the cash market commitment being offset.

(v) Sales and purchases in referenced contracts described in paragraphs (a)(2)(i), (a)(2)(ii), (a)(2)(iii), and (a)(2)(iv) of this section may also be offset other than by the same quantity of the same cash commodity, *provided that* the fluctuations in value of the position in referenced contracts are substantially related to the fluctuations in value of the actual or anticipated cash position, and *provided that* the positions shall not be maintained during the five last trading days of any referenced contract.

(b) *Information on cash market commodity activities.* Any trader with a position that exceeds the position limits set forth in § 151.4 pursuant to paragraph (a) of this section shall submit to the Commission a 404 filing, in the form and manner provided for in § 151.10, containing the following information with respect to such position:

(1) The cash market commodity hedged, the units in which it is measured, and the corresponding referenced contract that is used for hedging the cash market commodity;

(2) The number of referenced contracts used for hedging;

(3) The entire quantity of stocks owned of the cash market commodity that is being hedged by a position in a referenced contract;

(4) The entire quantity of open fixed price purchase commitments in the hedged commodity outside of the spot month of the corresponding referenced contract;

(5) The entire quantity of open fixed price purchase commitments in the hedged commodity in the spot month of the corresponding referenced contract;

(6) The entire quantity of open fixed price sale commitments in the hedged commodity outside of the spot month of the corresponding referenced contract; and

(7) The entire quantity of open fixed price sale commitments in the hedged commodity in the spot month of the corresponding referenced contract.

(c) *Anticipatory hedge exemptions.*

(1) *Initial statement.* Any trader who wishes to exceed the position limits set forth in § 151.4 pursuant to paragraph (a) of this section in order to hedge unsold anticipated commercial production or unfilled anticipated commercial requirements connected to a commodity underlying a referenced contract, shall submit to the Commission a 404A filing at least ten days in advance of the date that such transactions or positions would be in excess of the position limits set forth in § 151.4. The 404A filing shall be made

in the form and manner provided in § 151.10 and shall contain the following information with respect to such position:

(i) The cash market commodity and units for which the anticipated production or requirements pertain;

(ii) The dates for the beginning and end of the period for which the person claims the anticipatory hedge exemption is required, which may not exceed one year;

(iii) The production or requirement of that cash market commodity for the three complete fiscal years preceding the current fiscal year;

(iv) The anticipated production or requirements for the period hedged, which may not exceed one year;

(v) The unsold anticipated production or unfilled anticipated requirements across the period hedged, which may not exceed one year;

(vi) The referenced contract that the trader will use to hedge the unfilled, anticipated production or requirements; and

(vii) The number of referenced contracts that will be used for hedging.

(2) *Approval.* All or a specified portion of the unsold anticipated production or unfilled anticipated requirements described in these filings shall not be considered as offsetting positions for *bona fide* hedging transactions or positions if such person is so notified by the Commission within ten days after the Commission is furnished with the information required under this paragraph (c).

(i) The Commission may request the person so notified to file specific additional information with the Commission to support a determination that the statement filed accurately reflects unsold anticipated production or unfilled anticipated requirements.

(ii) The Commission shall consider all additional information filed and, by notice to such person, shall specify its determination as to what portion of the production or requirements described constitutes unsold anticipated production or unfilled anticipated requirements for the purposes of *bona fide* hedging.

(3) *Supplemental reports.* Whenever the sales or purchases which a person wishes to consider as *bona fide* hedging of unsold anticipated production or unfilled anticipated requirements shall exceed the amounts in the most recent filing or the amounts determined by the Commission to constitute unsold anticipated production or unfilled anticipated requirements pursuant to paragraph (c)(2) of this section, such person shall file with the Commission a statement which updates the

information provided in the person's most recent filing, and for instances anticipated needs exceed the amounts in the most recent filing, at least ten days in advance of the date that person wishes to exceed these amounts.

(d) *Additional information from swap counterparties to bona fide hedging transactions.* All persons that enter into swap transactions or maintain swap positions pursuant to paragraph (a)(1)(iv) of this section shall also submit to the Commission a 404S filing not later than 9:00 a.m. on the business day following that to which the information pertains. The 404S filing shall be done in the form and manner provided for in § 151.10 and shall contain the following information:

(1) The commodity reference price for the swaps that would qualify as a *bona fide* hedging transaction or position;

(2) The entire gross long and gross short quantity underlying the swaps that were executed in a transaction that would qualify as a *bona fide* hedging transaction, and the units in which the quantity is measured;

(3) The referenced contract that is used to offset the exposure obtained from the *bona fide* hedging transaction or position of the counterparty;

(4) The gross long or gross short size of the position used to offset the exposure obtained from a *bona fide* hedging transaction or position of the counterparty;

(5) The gross long or gross short size of the position used to offset the exposure obtained from a *bona fide* hedging swap transaction or position that is in the spot month.

(e) *Recordkeeping.* Traders who qualify for *bona fide* hedge exemptions for cash market positions, anticipatory hedging, and swaps opposite counterparties that would qualify as *bona fide* hedging transactions or positions shall maintain complete books and records concerning all of their related cash, futures, and swap positions and transactions and make such books and records, along with a list of swap counterparties, available to the Commission upon request.

(f) *Conversion methodology for swaps not involving the same commodity.* In addition to the information required under this section, traders engaged in the hedging of commercial activity or positions resulting from swaps that are used for the hedging of commercial activity that does not involve the same quantity or commodity as the quantity or commodity associated with positions in referenced contracts that are used to hedge shall submit to the Commission a 404, 404A, or 404S filing, as

appropriate, containing the following information:

(1) Conversion information both in terms of the actual quantity and commodity used in the trader's normal course of business and in terms of the referenced contracts that are sold or purchased; and

(2) An explanation of the methodology used for determining the ratio of conversion between the actual or anticipated cash positions and the trader's positions in referenced contracts.

(g) *Requirements for bona fide hedging swap counterparties.* Upon entering into a swap transaction where at least one party is relying on a *bona fide* hedge exemption to exceed the position limits of § 151.4 with respect to such a swap:

(1) The party not hedging a cash market commodity risk, or both parties to the swap if both parties are hedging a cash market commodity risk, shall:

(i) Ask for a written representation from its counterparty verifying that the swap qualifies as a *bona fide* hedging transaction under paragraph (a)(1)(iv) of this section; and

(ii) Upon receipt of such written representation from the counterparty, provide written confirmation of such receipt to the counterparty.

(2) The party relying on the *bona fide* hedging exemption to enter into the swap transaction shall submit a written representation to its counterparty verifying that the swap qualifies as a *bona fide* hedging transaction, as defined in paragraph (a)(1)(iv) of this section.

(h) The written representation and receipt confirmation described in paragraph (g) of this section shall be retained by the parties to the swap and provided to the Commission upon request.

(i) *Filing requirement for bona fide hedgers.* Any party with cash market commodity risk relying on a *bona fide* hedging exemption to enter into and maintain a referenced contract position shall submit to the Commission a 404S filing, in the form and manner provided for in § 151.10, containing the information in paragraphs (b) and (c) of this section, for each business day on which such position was maintained, up to and including the day after the trader's position level is below the position limit that was exceeded.

(j) *Positions that are maintained.* For a swap that satisfies the requirements of paragraph (a) of this section, the party to whom the cash market commodity risk is transferred may itself establish, lift and re-establish a position in excess

of the position limits of § 151.4 provided that:

(1) The party and its counterparty comply with the requirements of paragraphs (g) through (i) of this section; and

(2) The party may only exceed such position limit to the extent and in such amounts that the qualifying swap directly offsets, and continues to offset, the cash market commodity risk of a *bona fide* hedging counterparty.

**§ 151.6 Position visibility.**

(a) *Visibility levels.* A trader holding or controlling, separately or in combination, net long or net short, referenced contracts in the following commodities when such positions in all months or in any single month (including the spot month) are in excess of the following position levels, shall comply with the reporting requirements of paragraphs (b) through (d) of this section:

VISIBILITY LEVELS FOR REFERENCED METALS CONTRACTS

<i>New York Mercantile Exchange Copper (HG)</i> .....	4,200
<i>New York Mercantile Exchange Palladium (PA)</i> .....	900
<i>New York Mercantile Exchange Platinum (PL)</i> .....	1,400
<i>New York Mercantile Exchange Gold (GC)</i> .....	10,700
<i>New York Mercantile Exchange Silver (SI)</i> .....	4,500

VISIBILITY LEVELS FOR REFERENCED ENERGY CONTRACTS

<i>New York Mercantile Exchange Light Sweet Crude Oil (CL)</i> .....	22,500
<i>New York Mercantile Exchange New York Harbor Gasoline Blendstock (RB)</i> .....	7,800
<i>New York Mercantile Exchange Henry Hub Natural Gas (NG)</i> ...	21,000
<i>New York Mercantile Exchange New York Harbor No. 2 Heating Oil (HO)</i> .....	9,900

(b) *Statement of trader exceeding visibility level.* Upon acquiring a position in referenced contracts in the same commodity that reaches or exceeds a visibility level, a trader shall submit to the Commission a 401 filing for the position in a referenced contract, separately by futures, options, swaps, or swaptions that comprise the position in the form and manner provided for in § 151.10, and shall containing the following information:

(1) The date on which the trader's position initially reached or exceeded the visibility level;

(2) Gross long and gross short positions on an all-months-combined basis (using economically reasonable and analytically supported deltas);

(3) If the visibility levels are reached or exceeded in any single month, the contract month and the trader's gross long and short positions in the relevant single month (using economically reasonable and analytically supported deltas); and

(4) If applicable, the trader shall also certify that they do not hold or control positions subject to the filing requirements of paragraphs (c) and (d) of this section.

(c) *Related uncleared swaps position report.* Upon acquiring a position in referenced contracts in the same commodity that reaches or exceeds a visibility level, a trader shall submit to the Commission a 402S filing for any uncleared swap positions that are based on substantially the same commodity as that which underlies the referenced contract. The 402S filing shall be done in the form and manner provided for in § 151.10 and shall contain the following information for the date on which the trader's position initially reached or exceeded the visibility level:

(1) By commodity reference price;  
 (2) By swaps or swaptions;  
 (3) By open swap end dates within 30 days, 90 days, one year or outside of one year from the date on which the trader's position initially reached or exceeded the visibility level; and

(4) Gross long and gross short positions on a futures equivalent basis in terms of the referenced contract; or

(5) With the express written permission of the Commission or its designees, the submission of a swaps portfolio summary statement spreadsheet in digital format, only insofar as the spreadsheet provides at least the same data as that required by the 402S filing, may be substituted for the reporting requirements of the 402S filing.

(d) Any trader above a visibility level that holds or controls cash market commodity positions or has anticipated commercial requirements or unsold anticipated commercial production in the same or substantially the same commodity shall submit to the Commission 404 and 404A filings respectively. Such 404 and 404A filings shall be done in the form and manner provided for in § 151.10 and shall contain information regarding such positions as described in § 151.5(b) and (c). Notwithstanding this requirement, a visible trader may alternatively, upon written permission by the Commission or its designees, submit in digital format a physical commodity portfolio

summary statement spreadsheet, provided that such spreadsheet contains at least the same data as that required by the 404 or 404A filing.

(e) Reporting obligations imposed by regulations other than those contained in this section shall supersede the reporting requirements of paragraphs (b), (c), and (d) of this section but only insofar as other reporting obligations provide at least the same data and are submitted to the Commission or its designees at least as often as the reporting requirements of paragraphs (b), (c), and (d) of this section.

#### **§ 151.7 Aggregation of positions.**

(a) *Positions to be aggregated.* The position limits set forth in § 151.4 shall apply to all positions in accounts for which any trader by power of attorney or otherwise directly or indirectly holds positions or controls trading and to positions held by two or more traders acting pursuant to an expressed or implied agreement or understanding the same as if the positions were held by, or the trading of the position were done by, a single individual.

(b) *Ownership of accounts generally.* For the purpose of applying the position limits set forth in § 151.4, any trader holding positions in more than one account, or holding accounts or positions in which the trader by power of attorney or otherwise directly or indirectly has a 10 percent or greater ownership or equity interest, must aggregate all such accounts or positions.

(c) *Ownership by limited partners, shareholders or other pool participants.*

(1) Except as provided in paragraphs (c)(2) and (c)(3) of this section, a trader that is a limited partner, shareholder or other similar type of pool participant with an ownership or equity interest of 10 percent or greater in a pooled account or positions need not aggregate such pooled positions or accounts if:

(i) The pool operator has, and enforces, written procedures to preclude the trader from having knowledge of, gaining access to, or receiving data about the trading or positions of the pool;

(ii) The trader does not have direct, day-to-day supervisory authority or control over the pool's trading decisions; and

(iii) The pool operator has complied with the requirements of paragraph (g) of this section and has received an exemption from aggregation on behalf of the trader or a class of traders from the Commission.

(2) A commodity pool operator having ownership or equity interest of 10 percent or greater in an account or positions as a limited partner,

shareholder or other similar type of pool participant must aggregate those accounts or positions with all other accounts or positions owned or controlled by the commodity pool operator.

(3) Each limited partner, shareholder, or other similar type of pool participant having an ownership or equity interest of 25 percent or greater in a commodity pool must aggregate the pooled account or positions with all other accounts or positions owned or controlled by that trader.

(d) *Identical trading.* For the purpose of applying the position limits set forth in § 151.4, any trader that holds or controls the trading of positions, by power of attorney or otherwise, in more than one account, or that holds or controls trading of accounts or positions in multiple pools, with identical trading strategies must aggregate all such accounts or positions.

(e) *Trading control by futures commission merchants.* The position limits set forth in § 151.4 shall be construed to apply to all positions held by a futures commission merchant or its separately organized affiliates in a discretionary account, or in an account which is part of, or participates in, or receives trading advice from a customer trading program of a futures commission merchant or any of the officers, partners, or employees of such futures commission merchant or its separately organized affiliates, unless:

(1) A trader other than the futures commission merchant or the affiliate directs trading in such an account;

(2) The futures commission merchant or the affiliate maintains only such minimum control over the trading in such an account as is necessary to fulfill its duty to supervise diligently trading in the account;

(3) Each trading decision of the discretionary account or the customer trading program is determined independently of all trading decisions in other accounts which the futures commission merchant or the affiliate holds, has a financial interest of 10 percent or more in, or controls; and

(4) The futures commission merchant has complied with the requirements of paragraph (g) of this section and has received an exemption from aggregation from the Commission.

(f) *Owned non-financial entities.* An entity need not aggregate its positions with the positions of one of its owned non-financial entities, as defined in § 151.1, if it can sufficiently demonstrate, in an application for exemption submitted under paragraph (g) of this section, that the owned non-financial entity's trading is

independently controlled and managed, indicia of which include:

(1) The entity and its other affiliates have no knowledge of trading decisions by the owned non-financial entity, and the owned non-financial entity has no knowledge of trading decisions by the entity or any of the entity's other affiliates;

(2) The owned non-financial entity's trading decisions are controlled by persons employed exclusively by the owned non-financial entity, who do not in any way share trading control with persons employed by the entity;

(3) The owned non-financial entity maintains and enforces written policies and procedures to preclude the entity or any of its affiliates from having knowledge of, gaining access to, or receiving information or data about its positions, trades or trading strategies, including document routing and other procedures or security arrangements; and

(4) The owned non-financial entity maintains a risk management system that is separate from the risk management system of the entity and any of its other affiliates.

(5) Any other factors the Commission may consider, in its discretion, that indicate that the owned non-financial entity's trading is independently controlled and managed.

(g) *Applications for exemption.* (1) Entities seeking an exemption from the position limits established by the Commission pursuant to this section, shall file an initial application for an exemption providing as part of the application all information required by the Commission, including but not limited to information:

(i) Describing the relevant circumstances that warrant disaggregation;

(ii) Providing an independent assessment report on the operation of the policies and procedures described in § 151.9(c)(1)(iii) for pool operators and § 151.9(f)(3) for owned non-financial entities;

(iii) Designating an office and employee(s) of the entity, with salaries and compensation that are independent of trading profits and losses, which shall be responsible for the coordination of aggregation rules and position limit compliance;

(iv) Providing an organizational chart that includes the name, main business address, main business telephone number, main facsimile number and main e-mail address of the entity and each of its affiliates;

(v) Providing the names of pertinent employees of the entity (trading, operations, compliance, risk

management and legal) and their work locations and contact information;

(vi) Providing a description of all information-sharing systems, bulletin boards, and common e-mail addresses;

(vii) Providing an explanation of the entity's risk management system;

(viii) Providing an explanation of how and to whom the trade data and position information is distributed, including which officers receive reports and their respective titles; and

(ix) A signature by a representative duly authorized to bind the entity.

(2) An application shall be submitted within the time specified by the Commission and in the form and manner provided for in § 151.10.

#### § 151.8 Foreign boards of trade.

The aggregate position limits in § 151.4 shall apply to a trader with positions in referenced contracts executed on, or pursuant to the rules of a foreign board of trade, provided that:

(a) Such referenced contracts settle against the price (including the daily or final settlement price) of one or more contracts listed for trading on a registered entity; and

(b) The foreign board of trade makes available such referenced contracts to its members or other participants located in the United States through direct access to its electronic trading and order matching system.

#### § 151.9 Preexisting positions.

(a) The position limits set forth in § 151.2 of this chapter may be exceeded to the extent that such positions remain open and were entered into in good faith prior to the effective date of any rule, regulation, or order that specifies a position limit under this part.

(b) Swap and swaption positions entered into in good faith prior to the effective date of any rule, regulation, or order that specifies a position limit under this part may be netted with post-effective date swap and swaptions for the purpose of applying any position limit.

(c) Swap and swaption positions entered into in good faith prior to the effective date of any rule, regulation or order that specifies a position limit under this part shall not be aggregated with positions in referenced contracts that were entered into after the effective date of such a rule, regulation or order.

#### § 151.10 Form and manner of reporting and submitting information or filings.

Unless otherwise instructed by the Commission or its designees, any person submitting reports under this section shall submit the corresponding required filings and any other information

required under this part to the Commission as follows:

(a) Using the format, coding structure, and electronic data transmission procedures approved in writing by the Commission; and

(b) Not later than 9 a.m. on the next business day following the reporting or filing obligation is incurred *unless*:

(1) A 404A filing is submitted pursuant § 151.5(c), in which case the filing must be submitted at least ten days in advance of the date that transactions and positions would be established that would exceed a position limit set forth in § 151.4;

(2) A 404 or 404S filing is submitted pursuant to § 151.5, in which case the filing must be submitted the day after a position limit is exceeded and all days the trader exceeds such levels and the first day after the trader's position is below the position limit;

(3) The filing is submitted pursuant to § 151.6 and not under any other part under this title, then the 401, 402S, 404, or 404A filing, or their respective substitutes as provided for under § 151.6(c)(5) and (d), shall be submitted after the establishment of a position exceeding a visibility level on the latter of either (i) 9 a.m. five business day after such time or (ii) 9 a.m. the first business day of the subsequent calendar month. If the filing is submitted pursuant to § 151.6 and not under any other part under this title, the filing trader shall be required to submit a 401, 402S, 404, or 404A filing, or their respective substitutes, no more often than once per calendar month; or

(4) An application for exemption renewal is filed pursuant to § 151.7(g)(1), in which case the filing shall be submitted within 30 calendar days of January 1 of each year following the initial application for exemption.

#### § 151.11 Registered entity position limits.

(a) *Generally.* (1) Registered entities shall adopt, and establish rules and procedures for monitoring and enforcing spot-month, single-month, and all-months-combined position limits with respect to agreements, contracts or transactions executed pursuant to their rules that are no greater than the position limits specified in § 151.4.

(2) For agreements, contracts or transactions with no Federal limits, or with respect to levels of open interest to which no Federal limits apply, registered entities that are trading facilities shall adopt spot-month, single-month and all-months-combined position limits based on the methodology in 151.4, *provided, however*, that a registered entity may adopt, notwithstanding the

methodology in 151.4, single-month or all-months-combined limit levels of 1,000 contracts for tangible commodities other than energy products and 5,000 contracts for energy products and non-tangible commodities, including contracts on financial products.

(3) Securities futures products.

Position limits for securities futures products are specified in Part 41.

(b) *Alternatives.* For a contract that is not subject to a Federal position limit, registered entities may adopt position accountability rules with respect to any agreement, contract or transaction:

(1) On a major foreign currency, for which there is no legal impediment to delivery and for which there exists a highly liquid cash market; or

(2) On an excluded commodity that is an index or measure of inflation, or other macroeconomic index or measure; or

(3) On an excluded commodity that meets the definition of section 1.13(ii), (iii), or (iv) of the Act; or

(4) On an excluded commodity having an average open interest of 50,000 contracts and an average daily trading volume of 100,000 contracts and a highly liquid cash market.

(c) *Aggregation.* Position limits or accountability rules established under this section shall be subject to the aggregation standards of § 151.7.

(d) *Exemptions.* (1) *Hedge exemptions.* (i) For purposes of exempt and agricultural commodities, no designated contract market or swap execution facility bylaw, rule, regulation, or resolution adopted pursuant to this section shall apply to any position that would otherwise be exempt from the applicable Federal speculative position limits as determined by § 151.5; *provided, however*, that the designated contract market or swap execution facility may limit *bona fide* hedging positions or any other positions which have been exempted pursuant to § 151.5 which it determines are not in accord with sound commercial practices or exceed an amount which may be established and liquidated in an orderly fashion.

(ii) For purposes of excluded commodities, no designated contract market or swap execution facility bylaw, rule, regulation or resolution adopted pursuant to this section shall apply to any transaction or position defined under § 1.3(z); *provided, however*, that the designated contract market or swap execution facility may limit *bona fide* hedging positions which it determines are not in accord with sound commercial practices or exceed an amount which may be established and liquidated in an orderly fashion.



(2) *Procedure.* Persons seeking to establish eligibility for an exemption must comply with the procedures of the designated contract market or swap execution facility for granting exemptions from its speculative position limit rules. In considering whether to permit or grant an exemption, a contract market or swap execution facility must take into account sound commercial practices and paragraph (d)(1) of this section apply principles while remaining consistent with § 151.5.

(f) *Other exemptions.* Speculative position limits adopted pursuant to this section shall not apply to:

(1) any position acquired in good faith prior to the effective date of any bylaw, rule, regulation, or resolution which specifies such limit; or

(2) any person that is registered as a futures commission merchant or as a

floor broker under authority of the Act, except to the extent that transactions made by such person are made on behalf of or for the account or benefit of such person.

(g) *Ongoing responsibilities.* Nothing in this Part shall be construed to affect any provisions of the Act relating to manipulation or corners or to relieve any designated contract market, swap execution facility, or governing board of a designated contract market or swap execution facility from its responsibility under other provisions of the Act and regulations.

**§ 151.12 Delegation of authority to the Director of the Division of Market Oversight.**

(a) The Commission hereby delegates, until it orders otherwise, to the Director of the Division of Market Oversight or such other employee or employees as

the Director may designate from time to time, the authority:

(1) In § 151.4(e) for determining levels of open interest;

(2) In § 151.5 for granting exemptions relating to *bona fide* hedging transactions; and

(3) In § 151.10 for providing instructions or determining the format, coding structure, and electronic data transmission procedures for submitting data records and any other information required under this part.

(b) The Director of the Division of Market Oversight may submit to the Commission for its consideration any matter which has been delegated in this section.

(c) Nothing in this section prohibits the Commission, at its election, from exercising the authority delegated in this section.

APPENDIX A TO PART 151

Contract	Spot month	
	Current federal limit	Current exchange limit
<b>Agricultural Contracts</b>		
Cocoa .....		1,000
Coffee .....		500
Corn .....	600	600
Cotton No. 2 .....	300	300
Feeder Cattle .....		300
Frozen Concentrated Orange Juice .....		300
Lean Hogs .....		950
Live Cattle .....		450
Milk Class III .....		1,500
Oats .....	600	600
Rough Rice .....		600
Soybeans .....	600	600
Soybean Meal .....	720	720
Soybean Oil .....	540	540
Sugar No. 11 .....		5,000
Sugar No. 16 .....		1,000
Wheat (CBOT) .....	600	600
Wheat, Hard Red Spring .....	600	600
Wheat, Hard Winter .....	600	600
<b>Base Metals Contracts</b>		
Copper Grade #1 .....		1,200
<b>Precious Metals Contracts</b>		
Gold .....		3,000
Palladium .....		650
Platinum .....		150
Silver .....		1,500
<b>Energy Contracts</b>		
Crude Oil, Light Sweet ("WTI") .....		3,000
Gasoline Blendstock (RBOB) .....		1,000
Natural Gas .....		1,000
No. 2 Heating Oil, New York Harbor .....		1,000

Issued by the Commission, this 13th day of January 2011, in Washington, DC.

**David Stawick,**

*Secretary of the Commission.*

### **Appendices to Position Limits for Derivatives—Commission Voting Summary and Statements of Commissioners**

**Note:** The following appendices will not appear in the Code of Federal Regulations

#### **Appendix 1—Commission Voting Summary**

On this matter, Chairman Gensler and Commissioners Dunn, Chilton and O'Malia voted in the affirmative; Commissioner Sommers voted in the negative.

#### **Appendix 2—Statement of Chairman Gary Gensler**

I support the proposed rulemaking to establish position limits for physical commodity derivatives. The CFTC does not set or regulate prices. Rather, the Commission is directed to ensure that commodity markets are fair and orderly to protect the American public.

When the CFTC set position limits in the past, the agency sought to ensure that the markets were made up of a broad group of market participants with a diversity of views. At the core of our obligations is promoting market integrity, which the agency has historically interpreted to include ensuring markets do not become too concentrated.

Position limits help to protect the markets both in times of clear skies and when there is a storm on the horizon. In 1981, the Commission said that “the capacity of any contract market to absorb the establishment and liquidation of large speculative positions in an orderly manner is related to the relative size of such positions, i.e., the capacity of the market is not unlimited.”

Today's proposal would implement important new authorities in the Dodd-Frank Act to prevent excessive speculation and manipulation in the derivatives markets. The Dodd-Frank Act expanded the scope of the Commission's mandate to set position limits to include certain swaps. The proposal re-establishes position limits in agriculture, energy and metals markets. It includes one position limits regime for the spot month and another regime for single-month and all-months combined limits. It would implement spot-month limits, which are currently set in agriculture, energy and metals markets,

sooner than the single-month or all-months-combined limits. Single-month and all-months-combined limits, which currently are only set for certain agricultural contracts, would be re-established in the energy and metals markets and be extended to certain swaps. These limits will be set using the formula proposed today based upon data on the total size of the swaps and futures market collected through the position reporting rule the Commission hopes to finalize early next year. It is only with the passage and implementation of the Dodd-Frank Act that the Commission will have broad authority to collect data in the swaps market.

It will be some time before position limits for single-month and all-months-combined can be fully implemented. In the interim, if a trader has a position that is above a level of 10 and 2½ percent of futures and options on futures open interest in the 28 contracts for which the Commission is proposing position limits, I have directed staff to collect information, including using special call authority when appropriate, to monitor these large positions. Staff will brief the Commission and make any appropriate recommendations based upon existing authorities for the Commission's consideration during its closed surveillance meetings at least monthly on what staff finds.

Collecting this data relating to large traders with positions in the futures markets above such levels or points of 10 and 2½ percent would give the Commission a better look into the market and help us identify potential concerns. For example, if a trader does not have a bona fide hedge exemption, we can look into the details of its position and its intentions. It may also give us additional information as to how the position limits in the proposed rulemaking would affect traders in these markets.

These levels, or points, are the positions at which CFTC staff will brief the Commission under its existing authorities. They would not be a substitute for current position limits or accountability levels, and they should not be interpreted to be a level that will automatically trigger any additional regulatory action.

#### **Appendix 3—Statement of Commissioner Bart Chilton**

I reluctantly concur in the Commission's approval of publication of notice of a proposed rulemaking on position limits for derivatives. I support the Commission's issuance of a position limits proposal, but I do not support the timing.

I have said repeatedly that it is of paramount importance to adhere to the

deadlines imposed by Congress in the Wall Street Reform and Consumer Protection Act of 2010. Position limits is one of the rulemakings with an earlier target date. The current proposal does not meet the statutory time limits of imposition of limits within 180 days from the date of enactment for energy and metal commodities and 270 days for agricultural commodities. The agency does not have the authority to delay these statutory deadlines.

At the open Commission meeting of the agency on December 9, 2010, the Chairman indicated an intent to move forward with two proposals on speculative position limits and to move “expeditiously” to implement spot month limits. This bifurcation of spot and single month/aggregate rulemakings was a good attempt to meet the January deadline set by Congress. At the meeting on December 16, 2010, however, the Commission was presented with a single proposed rule, with a 60-day comment period, addressing spot, single month, and aggregate limits. Accordingly, it is now clear that spot month limits will not be implemented for many months, at best, and single month/aggregate limits—and the corresponding new bona fide hedging rule—may take more than a year to implement.

We need to address excessive speculation in these markets now. We already have more speculative positions in the commodities markets than ever before. There are some who suggest that certain commodity prices are currently delinked from supply and demand fundamentals, and are being impacted by excessive speculation. Should these conditions worsen, I will not hesitate to continue to criticize the delay that the Commission's position limits proposed rulemaking exacerbates.

I commend the position point agreement that the Chairman publicly directed the staff to undertake. This interim measure will give the agency a window into the “largest of the large” traders in our markets, and is an appropriate provisional effort as we transition to include the swaps market into our traditional surveillance systems.

The Commission should have acted so as to implement position limits as directed by Congress, pursuant to the statutory deadlines. I am disappointed that it failed to do so, and I will continue to aggressively advocate for rules that will appropriately address excessive speculation

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