



# Federal Register

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**Friday,  
December 12, 2008**

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## **Part III**

# **Commodity Futures Trading Commission**

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**17 CFR Parts 15, 16, 17, et al.  
Significant Price Discovery Contracts on  
Exempt Commercial Markets; Proposed  
Rule**

## COMMODITY FUTURES TRADING COMMISSION

17 CFR Parts 15, 16, 17, 18, 19, 21, 36, and 40

### Significant Price Discovery Contracts on Exempt Commercial Markets

**AGENCY:** Commodity Futures Trading Commission.

**ACTION:** Proposed rules.

**SUMMARY:** The Commodity Futures Trading Commission (“Commission” or “CFTC”) is proposing rules to implement the CFTC Reauthorization Act of 2008 (“Reauthorization Act”).<sup>1</sup> In pertinent part, the Reauthorization Act amends the Commodity Exchange Act to significantly expand the CFTC’s regulatory authority over exempt commercial markets (“ECMs”), which had heretofore operated largely outside the Commission’s regulatory reach, by creating a new regulatory category—ECMs with significant price discovery contracts (“SPDCs”)—and directing the Commission to adopt rules to implement this expanded authority. In addition to proposing regulations mandated by the Reauthorization Act, the Commission is also proposing to amend existing regulations applicable to registered entities in order to clarify that such regulations are now applicable to ECMs with SPDCs.

**DATES:** Comments must be received by February 10, 2009.

**ADDRESSES:** You may submit comments by any of the following methods:

- *Federal eRulemaking Portal:* <http://www.regulations.gov>.
- *Mail/Hand Deliver:* David Stawick, Secretary of the Commission, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW., Washington, DC 20581.
- *E-mail:* [secretary@cftc.gov](mailto:secretary@cftc.gov).

#### FOR FURTHER INFORMATION CONTACT:

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### I. Background

#### A. The Commodity Futures Modernization Act of 2000 Established a New Regulatory Framework

##### 1. Multi-Tiered Regulation

On December 21, 2000, Congress enacted the Commodity Futures Modernization Act (“CFMA”), which amended the Commodity Exchange Act (“Act” or “CEA”) to replace the Act’s “one-size-fits-all” supervisory framework for futures trading with a multi-tiered approach to regulatory oversight of derivatives markets. The CFMA applies different levels of regulatory oversight to markets based primarily on the nature of the underlying commodity being traded and the participants who are trading. In general, the more sophisticated the traders or commercial participants, or the less susceptible a commodity is to manipulation or other market or trading abuses, the less regulatory oversight is required under the CFMA.

Accordingly, designated contract markets (“DCMs”), are subject to the highest level of regulatory oversight because they are open to all participants and may offer all types of commodities.<sup>3</sup> Derivatives Transaction Execution

Facilities (“DTEFs”)<sup>4</sup> are subject to less regulatory oversight than DCMs because participants must be sophisticated investors or must be hedging risk associated with their commercial activities. Additionally, the CFMA imposes limitations on the types of commodities that may be traded, and the manner in which they may be traded.<sup>5</sup> Exempt Boards of Trade (“EBOTs”) are subject to virtually no regulatory oversight and are not registered with or designated by the Commission. EBOTs are exempt from most provisions of the CEA other than its antifraud and anti-manipulation prohibitions, but are subject to significant commodity and participant restrictions.<sup>6</sup> In addition to creating these three new categories of trading facility, the CFMA created a broad array of exclusions and exemptions from regulation for certain swaps and other derivatives products traded either bilaterally or on electronic trading facilities.<sup>7</sup> These exclusions and exemptions reflected a view, consistent with Congressional and Commission actions relating to the passage of the CFMA, that transactions between sophisticated counterparties do not necessarily require the protections that the CEA provides for transactions on DCMs and DTEFs.

##### 2. Exempt Commercial Markets

The CFMA established an exemption for transactions in exempt commodities traded on electronic trading facilities, also known as exempt commercial markets (“ECMs”).<sup>8</sup> To qualify as an ECM, a facility must limit its transactions to principal-to-principal transactions executed between “eligible commercial entities” (“ECEs”) on an “electronic trading facility.”<sup>10</sup> Contracts

<sup>4</sup> To qualify as a DTEF, an exchange must implement certain restrictions on retail market participation and can only trade certain commodities (including excluded commodities and other commodities with very high levels of deliverable supply) and generally must exclude retail participants. *CFTC Glossary (Glossary)*.

<sup>5</sup> 7 U.S.C. 7a.

<sup>6</sup> EBOTs may trade only “excluded commodities” (7 U.S.C. 1a(13); 17 CFR § 36.2(a)(2)(i)), and are open only to “eligible contract participants” (“ECPs”) (7 U.S.C. 1a(12)).

<sup>7</sup> For example, section 2(g) created an exclusion from the CEA for individually negotiated swaps, based on non-agricultural commodities entered into between eligible contract participants, 7 U.S.C. 2(g). Similarly excluded are transactions between ECPs involving excluded commodities that are not executed on a trading facility. 7 U.S.C. 2(d)(1).

<sup>8</sup> 7 U.S.C. 2(h)(3)–(5).

<sup>9</sup> 7 U.S.C. 1a(11) (a subset of ECPs).

<sup>10</sup> 7 U.S.C. 1a(10). For purposes of this proposed rulemaking, the terms electronic trading facility and ECM are used interchangeably. The term “trading facility” means a person or group of persons that constitutes, maintains, or provides a physical or

<sup>1</sup> Incorporated as Title XIII of the Food, Conservation and Energy Act of 2008, Pub. L. No. 110-246, 122 Stat. 1624 (June 18, 2008).

<sup>2</sup> 7 U.S.C. 1 *et seq.*

<sup>3</sup> 7 U.S.C. 7.

for all commodities except agricultural and excluded commodities (primarily financial commodities but also commodities such as weather) potentially are eligible to trade on an ECM. Examples of commodities traded on ECMs are energy products, metals, chemicals, air emission allowances, paper pulp, and barge freight rates.<sup>11</sup> ECMs fall somewhere between DTEFs and EBOTs on the regulatory oversight spectrum. Like EBOTs, they are neither licensed nor registered with the CFTC and are subject to the Act's antifraud and anti-manipulation provisions.<sup>12</sup> In addition, and different from EBOTs, ECMs are subject to certain recordkeeping and reporting requirements under the CEA.<sup>13</sup>

### 3. Differences Between ECMs and DCMs

ECMs are not subject to the level of transparency and Commission oversight associated with DCMs. DCMs must satisfy specified criteria to become designated, and then must demonstrate continuing compliance with 18 core principles set out in the Act.<sup>14</sup> The Act provides flexibility with respect to how DCMs may choose to meet the core

electronic facility or system in which multiple participants have the ability to execute or trade agreements, contracts or transactions—(i) by accepting bids or offers made by other participants that are open to multiple participants in the facility or system; or (ii) through the interaction of multiple bids or multiple offers within a system with a predetermined non-discretionary automated trade matching and execution algorithm. 7 U.S.C. 1a(34).

<sup>11</sup> 7 U.S.C. 1a(14).

<sup>12</sup> Sections 2(h)(4)(B) and (C) of the Act, 7 U.S.C. 2(h)(4)(B) and (C).

<sup>13</sup> For example, an ECM must maintain for five years and make available for inspection records of its activities relating to its business as a trading facility. 7 U.S.C. 2(h)(5)(B)(ii). More specifically, Commission rule 36.3, 17 CFR 36.3, requires that an ECM identify to the Commission those transactions for which it intends to rely on the exemption in section 2(h)(3) of the CEA and which averaged five trades per day or more over the most recent calendar quarter. For all such transactions, the ECM must provide to the Commission weekly reports showing certain basic trading information, or provide the Commission with electronic access that would allow it to compile the same information. 17 CFR 36.3(b)(1)(ii). An ECM also must provide to the Commission, upon special call, any information relating to its business that the Commission determines is appropriate to enforce the antifraud and anti-manipulation provisions of the CEA, to evaluate a systemic market event, or to obtain information on behalf of another federal financial regulator. 7 U.S.C. 2(h)(5)(B)(iii); 17 CFR 36.3(b)(3). An ECM must maintain a record of any allegations or complaints it receives concerning suspected fraud or manipulation and must provide the Commission with a copy of the record of each such complaint. 17 CFR 36.3(b)(1)(iii). Finally, an ECM is required to file an annual certification that it continues to operate in reliance on the exemption in section 2(h)(3) of the Act and that the information it previously provided to the Commission remains correct. 17 CFR 36.3(c)(4).

<sup>14</sup> See sections 5(d)(1)–(18) of the Act, 7 U.S.C. 7(d)(1)–(18).

principles' mandate that DCMs undertake significant supervisory responsibility with respect to trading on their markets. DCMs must, for example, establish rules and procedures for preventing market manipulation and must adopt necessary and appropriate position limit or accountability rules to address the potential for manipulation or congestion. DCMs also must establish compliance and surveillance programs, which the Commission evaluates through rule enforcement reviews,<sup>15</sup> and must monitor trading on their markets and must undertake other self-regulatory responsibilities mandated by the CEA.

The CFMA did not impose these obligations on ECMs. While the Commission was given the authority to determine whether an ECM performs a significant price discovery function for transactions in an underlying cash market,<sup>16</sup> such a determination did not trigger any self-regulatory responsibilities for the ECM or confer any additional oversight authority on the Commission. Rather, the presence of a contract performing a significant price discovery function required the ECM to publicly disseminate certain basic information, such as contract terms and conditions and daily trading volume, open interest, and opening and closing prices or price ranges.<sup>17</sup>

### B. The Changing ECM Landscape

Following enactment of the CFMA in December 2000, the first ECMs that notified the Commission of their intent to operate generally were simple trading platforms, resembling in many ways business-to-business facilities for large commercial firms. ECMs facilitate the execution of trades between commercial counterparties by offering an anonymous and efficient electronic matching system which many believed to be superior to the existing voice broker system, and to provide a competitive advantage over the bilateral OTC market, especially for energy products. Initially, most ECMs were

<sup>15</sup> The Commission conducts regular rule enforcement reviews of the self regulatory programs operated by DCMs for enforcing exchange rules, preventing market manipulations and customer and market abuses, and ensuring that trade related information is recorded and stored in a manner consistent with the Act.

<sup>16</sup> In 2004, the Commission amended its part 36 rules to include the requirement that an ECM notify the Commission when it has reason to believe that one or more of the markets on which it is conducting agreements, contracts or transactions in reliance on section 2(h)(3) of the CEA has been met or if the market holds itself out to the public as performing a price discovery function for the cash market of a commodity. 17 CFR 36.3(c)(2)(i) and (ii). 69 FR 43285 (July 20, 2004).

<sup>17</sup> *Id.*

small operations with low trading volumes that were small relative to DCMs. The first ECMs did not offer centralized clearing, but sought to address counterparty risk through the use of credit filters whereby traders could limit their potential counterparties to a list of traders whose credit they found satisfactory. Significantly, early ECM contracts were not linked to contracts listed on DCMs. Over time, however, ECMs began to offer "look-alike" contracts that were linked to the settlement prices of their exchange-traded counterparts, and these look-alike contracts in one case began to garner significant volumes. In recent years, several active ECMs began to offer the option of centralized clearing for their contracts—an option which became widely utilized by their customers to manage counterparty risk.

This evolution, and particularly the linkage of ECM contract settlement prices to DCM futures contract settlement prices, began to raise questions about whether ECM trading activity could impact trading on DCMs and whether the CFTC had adequate authority to address that impact and protect markets from manipulation and abuse. Of special concern to CFTC staff was the existence of the ECM cash-settled "look-alike" contracts that could provide an incentive to manipulate the settlement price of an underlying DCM futures contract to benefit positions in the look-alike ECM contract. As discussed more fully below, the Commission subsequently considered and studied these concerns in a variety of ways, culminating, in September 2007, in a public hearing examining trading on regulated exchanges and ECMs.<sup>18</sup>

### C. The CFTC's Response to the Changing Energy Markets

#### 1. Empirical Study of Trades on ICE<sup>19</sup> and NYMEX

During the last several years, one ECM in particular—the Intercontinental

<sup>18</sup> See Commodity Futures Trading Commission, *Report on the Oversight of Trading on Regulated Futures Exchanges and Exempt Commercial Markets* (October 2007), [http://www.cftc.gov/stellent/groups/public/@newsroom/documents/file/pr5403-07\\_ecmreport.pdf](http://www.cftc.gov/stellent/groups/public/@newsroom/documents/file/pr5403-07_ecmreport.pdf) for a comprehensive report of the Commission's findings following its September 2007 hearing ("ECM Report").

<sup>19</sup> Intercontinental Exchange, or ICE, consists of four separate entities: ICE OTC, to which this document refers, is an ECM trading energy products. ICE Future Europe trades energy futures and is regulated by the Financial Services Authority of Great Britain; ICE Futures US focuses primarily on futures based on soft commodities (e.g., coffee, sugar, cocoa, cotton) and financial futures and is regulated by the CFTC; ICE Futures Canada trades

Exchange (“ICE”)—has become a major trading venue for natural gas contracts in direct competition with the New York Mercantile Exchange (“NYMEX”) natural gas benchmark futures contract, in addition, Commission staff has found that the traders on ICE are virtually the same as the traders on NYMEX. All of the top 25 natural gas traders on NYMEX are also significant traders on ICE. For the Henry Hub natural gas market,<sup>20</sup> market participants generally view ICE and NYMEX as essentially a single market, looking to both ICE and NYMEX when determining where to execute a trade at the best price.

To assess these changes in the marketplace, the Commission’s Office of the Chief Economist (“OCE”) conducted an empirical study of the relationship between the natural gas contracts that trade on ICE and NYMEX. OCE collected transaction prices for ICE and NYMEX natural gas contracts from January 3, 2006 through December 31, 2006 and evaluated trading for 12 contract months when trading on each market was appropriately active. OCE examined the timing of price changes on ICE and NYMEX to draw inferences about where information arrives first. If price changes on one venue consistently “led” those on the other venue, then OCE concluded that informed traders preferred trading at that “leading” venue and inferred that market to be “discovering” prices.<sup>21</sup> OCE found that ICE exhibited price leadership with respect to NYMEX on 20 percent of the contract-days, while NYMEX exhibited price leadership on 63 percent of the contract-days. OCE concluded that these results suggested that both ICE and NYMEX are significant price discovery venues for natural gas futures contracts.

## 2. Commission Surveillance of the Energy Markets

The Commission’s surveillance of natural gas energy markets traditionally has focused on the regulated futures markets traded on NYMEX. Prior to the Reauthorization Act, ECMs were not subject to the requirements of the Commission’s large trader reporting system (“LTRS”).<sup>22</sup> In order to obtain

futures and options and is regulated by the Manitoba Securities Commission.

<sup>20</sup> Henry Hub is a natural gas pipeline hub in Louisiana that serves as the delivery point for NYMEX natural gas futures contracts and often serves as a benchmark for wholesale natural gas prices across the U.S. *Glossary*.

<sup>21</sup> See ECM Report at 11–12. Price discovery is the process of determining the price level for a commodity based on supply and demand conditions. Price discovery may occur in a futures market or cash market. *Glossary*.

<sup>22</sup> The LTRS is the centerpiece of the Commission’s market surveillance system. Under

analogous large trader information from ECMs, the Commission had to issue special calls.<sup>23</sup> Based on the prominent role played by the ICE natural gas contract in the price discovery process and the possible impact on the NYMEX natural gas contract, the Commission determined to issue a series of special calls for information related to ICE’s cleared natural gas swap contracts that are cash-settled based on the settlement price of the NYMEX physical delivery natural gas contract.<sup>24</sup>

## 3. The Commission’s ECM Hearing

Following the OCE study and the special calls issued to ICE, the Commission held a public hearing on September 18, 2007, to examine the oversight of DCMs and ECMs. Witnesses

the LTRS, clearing members, futures commission merchants and foreign brokers file daily reports with the CFTC showing futures and option positions in accounts they carry that are above reporting levels set by the Commission. The reporting level for the NYMEX natural gas futures market is 200 contracts.

<sup>23</sup> Section 2(h)(5)(B)(iii) of the Act, 7 U.S.C. 2(h)(5)(B)(iii), requires that an electronic trading facility relying on the exemption provided in section 2(h)(3) must, upon a special call by the Commission, provide such information related to its business as an electronic trading facility as the Commission may determine appropriate to enforce the antifraud provisions of the CEA, to evaluate a systemic market event, or to obtain information requested by a Federal financial regulatory authority in connection with its regulatory or supervisory responsibilities.

<sup>24</sup> The special calls were issued primarily to assist the Commission in its surveillance of the NYMEX natural gas contract. They were not issued as part of an investigation of any particular market participant or trading activity on either ICE or NYMEX, nor were they issued to conduct regular market surveillance of ICE. The first special call, issued on September 28, 2006, requested daily clearing member position data for ICE’s natural gas swap contracts, broken out between house and aggregate customer positions, which is similar to information that the Commission receives from NYMEX pursuant to Commission rule 16.00. This information permits CFTC market surveillance staff to see all cleared positions at the clearing member level, but it is not possible to determine individual customer positions. To obtain daily individual trader positions, the Commission issued a second special call on December 1, 2006. While the data received is similar to large trader reporting for DCMs, the methodology for reporting is very different. Because ICE is a principal-to-principal market and therefore does not receive position reporting from firms, it was necessary for ICE to develop an algorithm to infer open positions from the sum of all trading by each individual trader. While this approach has provided valuable information, it is less accurate than traditional large trader reporting. The third special call, issued on September 5, 2007, required ICE to provide all cleared transaction data for its Henry Hub swap contracts and identify counterparties for the final two trading sessions prior to the expiration of prompt month Henry Hub natural gas products. This data is similar to transaction data that the Commission receives from NYMEX for all trading days and enables CFTC staff to monitor trading activity on ICE and obtain more complete coverage to counter possible manipulative schemes that could affect trading on ICE.

at the hearing included Commission staff, representatives of DCMs and ECMs, and representatives of a broad spectrum of market users and consumer groups. The hearing focused on a number of issues, including the tiered regulatory approach of the CFMA and whether it was adequate; the similarities and differences between ECMs and DCMs; the associated regulatory risks of each market category; the types of regulatory or legislative changes that may be appropriate to address identified risks; and the impact that regulatory or legislative changes might have on the U.S. futures industry and the global competitiveness of the U.S. financial industry. In announcing the hearing, CFTC Acting Chairman Lukken observed that:

The evolution of these energy markets [ECMs] in recent years requires our agency to address whether the level of regulatory oversight is proper given the importance of energy prices to all Americans. \* \* \* This oversight hearing will provide a better understanding of the inter-relationship of these trading venues so policymakers can make informed decisions to protect these vital markets.<sup>25</sup>

## 4. The Commission’s Findings and Legislative Recommendations

Based on information developed through various studies, surveillance, special calls and its public hearing, the Commission published in October 2007 a “Report on the Oversight of Trading on Regulated Futures Exchanges and Exempt Commercial Markets.” (“ECM Report”).<sup>26</sup> The report was provided to the Commission’s Congressional oversight committees, which were then in the process of considering legislation to amend the CEA and reauthorize the Commission.

The ECM Report noted that while some participants disagreed, most witnesses at the September 18 hearing generally supported the tiered regulatory structure of the CFMA, but expressed concern regarding the regulatory provisions governing ECMs and the regulatory disparity between DCMs and ECMs.<sup>27</sup> Witnesses suggested that this disparity made markets more susceptible to manipulation and put regulated exchanges at a competitive disadvantage vis-à-vis ECMs offering virtually identical products. Generally, most witnesses felt that some changes to the ECM provisions might be appropriate, provided those changes

<sup>25</sup> CFTC Release 5368–07, August 2, 2007 (CFTC Announces September Hearing to Examine Trading on Regulated Exchanges and Exempt Commercial Markets).

<sup>26</sup> *supra* n. 20.

<sup>27</sup> *Id.* at 15.

were prudently targeted and did not adversely affect the ability of ECMs to innovate and grow.<sup>28</sup>

Based on the hearing testimony and its own experience in administering the Act, the Commission at that time concluded that the tiered approach of the CFMA generally had operated effectively. ECMs had proven popular for new start-up markets and had provided competition for DCMs, spurring them toward innovations of their own. The Commission further found that, to the extent that trading volume on an ECM contract remained low and its prices were not significantly relied upon by other markets, the current level of regulation remained appropriate. However, when a futures contract traded on an ECM matured and began to serve a significant price discovery function for transactions in commodities in interstate commerce, the contract warranted increased oversight to deter and prevent price manipulation or other disruptions to market integrity, both on the ECM itself and in any related futures contracts trading on DCMs. Such increased oversight would also help to ensure fair competition among ECMs and DCMs trading similar products and competing for the same business.

In light of these conclusions, the Commission's ECM Report recommended that the CEA be amended to grant the Commission additional authority over ECM contracts serving a significant price discovery function, and that certain self-regulatory responsibilities be assigned to ECMs offering such contracts. Specifically, the Commission advocated that (1) An ECM contract that is determined to perform a significant price discovery function be subject to large trader reporting requirements comparable to those applicable to all DCM contracts; (2) an ECM should be required to adopt position limits or accountability levels, as appropriate, for a listed contract that serves a significant price discovery function similar to the limits on DCMs; (3) an ECM should be required to monitor trading of a listed contract that serves a significant price discovery function to detect and prevent manipulation, price distortion, and disruptions of the delivery or cash-settlement process; and (4) the Commission and the ECM should be provided with emergency authority to alter or supplement contract rules, liquidate open positions, and suspend or curtail trading in any listed contract that serves a significant price discovery function. These authorities would be

essential tools for the Commission and the ECM to prevent manipulation and disruptions of the delivery or cash-settlement process.

The Commission further recommended that the determination whether an ECM contract serves a significant price discovery function should focus on the following factors: (1) *Material Liquidity*—trading volume in the ECM contract must be significant enough to affect regulated markets or to become a pricing benchmark; and (2) *Linkage/Material Price Reference*—the relevant ECM contract must either influence other markets and transactions through this linkage or be materially referenced by others in interstate commerce on a frequent and recurring basis.

#### *D. The Reauthorization Legislation and the Statutory Scheme*

The CFTC Reauthorization Act of 2008<sup>29</sup> adds a new section 2(h)(7) to the CEA to govern the treatment of “significant price discovery contracts” (“SPDCs”) on ECMs.<sup>30</sup> The legislation, based largely on the Commission's recommendations for improving oversight of ECMs, provides for greater regulation of contracts traded on ECMs that fulfill a significant price discovery function and establishes criteria for the Commission to consider in determining whether an ECM contract qualifies as a SPDC. The Reauthorization Act directs the CFTC to extend its regulatory oversight to the trading of SPDCs; requires ECMs to adopt position and accountability limits for SPDCs; authorizes the Commission to require large traders to report their positions in SPDCs; and establishes core principles for ECMs with contracts that are determined to perform a significant price discovery function. Finally, the legislation directs the Commission to issue rules implementing the provisions of new section 2(h)(7) of the CEA and to include in such rules the conditions under which an ECM will have the responsibility to notify the Commission that an agreement, contract or transaction conducted in reliance on the exemption provided in section 2(h)(3) of

the CEA may perform a price discovery function.<sup>31</sup>

The Reauthorization Act significantly broadens the CFTC's regulatory authority over ECMs by creating, in section 2(h)(7) of the CEA, a new regulatory category—ECMs on which SPDCs are traded—and treating electronic trading facilities in that category as registered entities subject to all provisions of the CEA that are applicable to registered entities.<sup>32</sup> The legislation confers on the CFTC the authority to designate an agreement, contract or transaction as a SPDC if the Commission determines, in its discretion, that the agreement, contract or transaction performs a significant price discovery function under criteria established by section 2(h)(7). When the Commission makes such a determination, the ECM on which the SPDC is traded must assume, with respect to that contract or contracts, all the responsibilities and obligations of a registered entity under the Act and Commission regulations, and must comply with nine core principles established by new section 2(h)(7)(C)—including the obligation to establish position limits and/or accountability standards for SPDCs.<sup>33</sup> The Reauthorization Act separately amends section 4i of the CEA to authorize the Commission to require large trader reports for SPDCs listed on ECMs.<sup>34</sup>

Consistent with Congress' directive, the Commission is issuing this proposed notice of rulemaking as an initial step to implementing the amended statutory scheme for ECMs with SPDCs.<sup>35</sup> These regulations are applicable to exempt markets, but also implicate parts 16 through 21 (market, transaction and large trader reporting rules), and 40 (provisions common to contract markets, derivatives transaction execution facilities and derivatives clearing organizations).

<sup>31</sup> Pub. L. 110–246 at sec. 12304. See also Conference Committee Report, at 985–86; 2008 Farm Bill Commodity Futures Title: Strengthening Oversight of Futures Markets, House Committee on Agriculture (May 9, 2008) [http://agriculture.house.gov/inside/Legislation/110/FB/Conf/Title\\_XIII\\_fs.pdf](http://agriculture.house.gov/inside/Legislation/110/FB/Conf/Title_XIII_fs.pdf).

<sup>32</sup> Conference Committee Report, at 985–86.

<sup>33</sup> Congress has made clear that an ECM with a SPDC shall be considered as a registered entity for purposes of the CEA. *Id.* at 985.

<sup>34</sup> Public Law 110–246 at sec. 13202.

<sup>35</sup> *Id.* at sec. 13204. Congress has directed that the Commission issue proposed rules implementing section 2(h)(7) of the CEA not later than 180 days after the date of enactment of the Reauthorization Act and that the Commission issue a final rule no later than 270 days after the date of enactment. The Reauthorization Act initially was enacted as H.R. 2419 on May 22, 2008 but was repealed due to clerical error—and concurrently enacted—by H.R. 2164, Public Law 110–264 on June 18, 2008.

<sup>29</sup> Public Law No. 110–246, *supra*, n. 1 (“Pub. L. 110–246”). The Reauthorization Act was incorporated into the Food, Conservation and Energy Act of 2008 as Title XIII of that legislation. Title XIII was not the subject of Congressional hearings and the legislative history is limited to The Joint Explanatory Statement of the Committee of Conference, H.R. Rep. No. 110–627, 110 Cong., 2d Sess. at 978–86 (2008) (Conference Committee Report).

<sup>30</sup> 7 U.S.C. 2(h)(7).

<sup>28</sup> *Id.*

## II. The Proposed Rules

### A. Part 36—Exempt Markets

Part 36 of the Commission's regulations contains the provisions that apply to exempt boards of trade and to exempt commercial markets, regardless of whether the markets are a significant source for price discovery. Rule 36.3 imposes a number of requirements and restrictions on ECMs—electronic trading facilities relying on the exemption in section 2(h)(3) of the CEA—including notification of intent to rely on the exemption; initial and ongoing information submission requirements; prohibited representations; price discovery notification; and price dissemination requirements. The Commission proposes to amend rule 36.3 to implement its broadened regulatory authority over ECMs with SPDCs under section 2(h)(7) of the CEA.

#### 1. Required Information

The notification provision in rule 36.3(a) is unchanged. The Commission proposes to amend rule 36.3(b) to separately specify the information submission requirements, both initially and on an ongoing basis, for: (1) All ECMs; (2) for ECMs with respect to agreements, contracts or transactions that have not been determined to perform a significant price discovery function; and (3) for ECMs with SPDCs.<sup>36</sup> The proposed amendment to rule 36.3(b) additionally includes provisions related to subpoenas, special calls and the delegation of authority and provides that an electronic trading facility relying on the exemption in section 2(h)(3) of the Act shall not, with respect to agreements, contracts or transactions that are not SPDCs, represent to any person that it is registered with, designated, recognized, licensed or approved by the Commission. This prohibition has its origin in section 2(h)(5) of the CEA, which sets forth the requirements and obligations for ECMs. Although the Reauthorization Act did not amend the prohibition on representation in section 2(h)(5)(7) of the Act, the legislation did amend the statutory definition of "registered entity" to include, "with respect to a contract that the Commission determines is a significant price discovery contract, any electronic trading facility on which the contract is executed or traded."<sup>37</sup> Accordingly, the Commission believes that when it has determined that a contract, agreement or

transaction executed or traded on the trading facility is a SPDC, the trading facility may represent that it is a registered entity, provided that the representation clearly and prominently states that the ECM is a registered entity only with respect to its SPDCs.

In general, the proposed information submission requirements for ECMs without SPDCs are drafted to be substantively similar to the information that all ECMs currently are required to provide.<sup>38</sup> A significant change to the submission requirements for ECMs is the proposed requirement to file, initially and on a quarterly basis, information about the terms and conditions as well as related information for all contracts traded on the facility. Although the proposed rules set forth the terms, standards and conditions under which an ECM will be responsible to notify the Commission that it may have a SPDC, the Commission is mindful that it must independently be aware of ECM contracts that may develop into SPDCs. The Commission believes that requiring ECMs to identify all agreements, contracts and transactions and to provide basic trading information will enable it to fulfill that obligation. To that end, the Commission proposes to retain for non-SPDCs the requirement that ECMs submit to the Commission weekly reports (or alternatively provide electronic access that would allow the Commission to capture the same information) for contracts that average five trades per day or more.<sup>39</sup> In addition, the Commission is proposing to add a quarterly reporting requirement for all non-SPDCs, to include their terms and conditions, average daily trading volume, and open interest. This quarterly reporting requirement also is being proposed to provide the Commission with information that will assist it in making prompt assessments whether ECM contracts may be SPDCs. ECMs should note that this provision will require them to fulfill the quarterly reporting requirement beginning with the end of the calendar quarter following the adoption of these final rules. Under proposed rule 36.3(b)(3), ECMs with SPDCs will be required to

comply with the daily reporting and publication requirements of regulation 16.01.<sup>40</sup>

#### 2. Identifying Significant Price Discovery Contracts

The Reauthorization Act directs the Commission to consider, as appropriate, four specific criteria when identifying whether an agreement, contract or transaction is a SPDC: Price linkage, arbitrage, material price reference, and material liquidity.<sup>41</sup> The legislation further directs that in its rulemaking to implement the provisions of section 2(h)(7) of the CEA, the Commission shall include the standards, as well as conditions under which an ECM will have the responsibility to notify the Commission that a contract traded on the facility may perform a significant price discovery function. Accordingly, proposed rule 36.3(c) addresses: (i) The criteria on which the Commission will rely in making a determination that an agreement, contract or transaction is a SPDC; (ii) the factors that will trigger the ECM's obligation to notify the Commission that it may have a SPDC; (iii) the procedures the Commission will follow in reaching its determination whether a contract is a SPDC (and in determining that a contract is no longer a SPDC); and (iv) the procedures and standards by which an ECM with a SPDC must demonstrate compliance with the core principles.

(i) *Criteria for SPDC Determination.* In enacting new section 2(h)(7) of the CEA, Congress specified four criteria that the Commission must consider in making a determination that an agreement, contract or transaction performs a significant price discovery function. Proposed rule 36.3(c)(1) enumerates the factors—price linkage, arbitrage, material price reference, and material liquidity. Because the legislation does not assign priority to any of the factors, and neither the statutory language nor the Conference Committee Report specifies the degree to which any of the factors must be present, section 2(h)(7)(B) gives the Commission flexibility in applying the criteria to a particular contract and market. The Commission is also mindful that:

[n]ot all the listed factors must be present to make a determination that a contract

<sup>36</sup> Enhanced obligations for ECMs with SPDCs apply only to the SPDCs and need not be applied to ECM contracts, agreements or transactions that are not SPDCs.

<sup>37</sup> Public Law 110–246 at sec. 13203(b)(3).

<sup>38</sup> ECMs that have already filed a Notification of Operation under section 2(h)(3) of the Act should note that proposed rule 36.3(b) will not require them to provide any additional information to the Commission explaining how the facility meets the definition of trading facility or with information demonstrating that the facility requires all participants to be ECEs as long as the operations of the facility and the participants trading on the facility have not materially changed since the filing of the notification or the most recent ECM Annual Certification form.

<sup>39</sup> See 17 CFR 36.3(b).

<sup>40</sup> Once in compliance with the core principles and daily reporting and publication requirements applicable to ECMs with SPDCs, ECMs will not be required to comply with proposed rule 36.3(b)(2) except in regard to non-SPDC contracts that are traded or executed on the facility.

<sup>41</sup> Section 2(h)(7)(B)(v) also authorizes the Commission to specify by rule other material factors relevant to a determination whether a contract is a SPDC.

performs a significant price discovery function. However, the Managers intend that the Commission should not make a determination that an agreement, contract or transaction performs a significant price discovery function on the basis of the price linkage factor unless the agreement, contract or transaction has sufficient volume to impact other regulated contracts or to become an independent price reference or benchmark that is regularly utilized by the public.<sup>42</sup>

Because the criteria mandated by Congress do not lend themselves to bright-line rules, the Commission proposes to explain, in Appendix A to the part 36 rules, how it expects to apply the criteria in making its determinations. This proposed guidance explains that the Commission will make SPDC determinations on a case-by-case basis, applying and weighing each factor as appropriate to the specific contract and circumstances under consideration; offers examples to illustrate which factor or combinations of factors the Commission would look to when evaluating whether a contract is performing a significant price discovery function; and describes the circumstances under which the presence of a factor or factors would be sufficient to warrant such a determination.

By way of example, for contracts that are linked to other contracts or that may be arbitrated with other contracts, the Commission would determine that the contract is a SPDC if the price of the contract moves in such harmony with the other contract that the two markets essentially become interchangeable. This co-movement of prices would be an indication that liquidity in the contract has reached a level sufficient for the contract to perform a significant price discovery function. Accordingly, the proposed guidance establishes threshold liquidity and price relationship standards that will inform the Commission's determination. A different approach is required when considering the price discovery potential of a contract that is serving as a material price reference. In these circumstances, the Commission would rely on either of two sources of evidence in making its determination. The Commission believes that a direct indicator that a contract is serving as a material price reference is observation that cash market participants are actively referencing the contract price

when they enter into cash market transactions. Routine publication of an ECM's contract price in widely distributed industry publications and newsletters also would indicate that industry participants attach some value to this information.

(ii) *Notification requirement for ECMs with a SPDC.* The Reauthorization Act requires that as part of its rulemaking to implement new section 2(h)(7) of the CEA, the Commission include the standards, terms and conditions under which an ECM will have the responsibility to notify the Commission that an agreement, contract or transaction conducted in reliance on the exemption provided in section 2(h)(3) of the CEA may perform a significant price discovery function.<sup>43</sup> Accordingly, in proposed rule 36.3(c)(2) the Commission has specified conditions, derived from the statutory criteria, which signal the ECM's obligation to notify the Commission of a possible SPDC. An ECM will be obligated to notify the Commission of a potential SPDC when an agreement, contract or transaction is traded an average of 5 trades per day or more over the most recent calendar quarter and also meets one of the other two reporting factors. The Commission is aware that this requirement may result in over-reporting by ECMs, and wishes to emphasize that the presence of one factor alone will not necessarily result in a determination that a contract is a SPDC. This notice requirement, however, will serve to alert the Commission to the contracts that are most likely to be SPDCs. The Commission believes that the benefit of having the maximum available information with which to make its determinations outweighs the costs associated with possible over-reporting by ECMs.

### 3. Procedures

When the Commission learns of a potential SPDC—whether through its own information collection and surveillance activities,<sup>44</sup> notification by an ECM pursuant to proposed rule 36.3(c)(2), or unsolicited information from participants in the cash market underlying a contract—the Reauthorization Act directs the Commission to implement a process for

determining whether ECM contracts are SPDCs. In proposed rule 36.3(c)(3) the Commission establishes procedures under which the Commission will make and announce its determination whether a particular contract performs a significant price discovery function and also sets forth the actions that must be taken by an ECM following such a determination. With respect to the former, proposed rule 36.3(c)(3) provides that when the Commission intends to undertake such a determination in response to notice by an ECM pursuant to rule 36.3(c)(2), or upon its own initiative, it will notice its intention in the **Federal Register**. The proposed rule also specifies that the Commission, as part of its consideration, will solicit written data, views and arguments from the ECM that lists the potential SPDC and from any other interested parties. Generally, such written submissions must be received within 30 calendar days of the date of publication in the **Federal Register**. After consideration of all relevant matters the Commission will issue an order explaining its determination. The issuance of an affirmative Commission order signals the effectiveness of the Commission's authorities with respect to ECMs with SPDCs<sup>45</sup> and triggers the obligations, requirements—both procedural and substantive—and timetables prescribed in proposed rule 36.3(c)(4) for the ECM.<sup>46</sup>

Under proposed rule 36.3(c)(4), an ECM with a SPDC must submit to the Commission a written demonstration that it complies with the nine core principles established in section 2(h)(7) of the CEA with respect to the SPDC. Although status as a registered entity attaches to an ECM as soon as the Commission issues its order determining that a particular ECM contract performs a significant price discovery function, the Commission has included in proposed rule 36.3(c)(4) a grace period for achieving compliance with the core principles. As proposed, the rule provides 90 calendar days for ECMs with a first-time determination of a SPDC to demonstrate compliance with

<sup>45</sup> Those authorities include the emergency powers conferred by section 8a(9) of the Act, 7 U.S.C. 12a(9), which permits the Commission to intervene when it has reason to believe an emergency exists and to take action necessary to maintain or restore orderly trading or liquidation of any futures contract.

<sup>46</sup> Should the Commission conclude, either formally or informally, that a contract which demonstrates some characteristics consistent with a SPDC nonetheless does not serve a significant price discovery function, the Commission may continue to monitor the contract pursuant to its special call authority under proposed rule 36.3(b)(1)(iv), and will advise the ECM as to what further reporting it may require with respect to the contract.

<sup>42</sup> Conference Committee Report at 984–85. In addition to the four criteria established by Congress, section 2(h)(7) permits the Commission to consider such other material factors as it may specify by rule as relevant to a determination whether an agreement, contract or transaction serves a significant price discovery function. 7 U.S.C. 2(h)(7)(B)(v).

<sup>43</sup> Public Law 110–246 at sec. 13204.

<sup>44</sup> The Reauthorization Act amended the CEA to require that the Commission review all ECM contracts at least once a year to determine whether any contract is a SPDC. In addition to these formal reviews, it is expected that Commission staff might also become aware of the price discovery attributes of ECM contracts in the ordinary course of discussion or interaction with ECM personnel and various cash and futures market participants.



the core principles.<sup>47</sup> For each subsequent SPDC, the ECM is given 15 calendar days from the date of the Commission's order to achieve compliance. The grace period is designed to ensure that the ECM has sufficient time to implement its new regulatory requirements and operations, while avoiding the market disruption that might occur by the sudden imposition of position limits and other trading rules. The Commission is aware that position limits that become effective at the end of the applicable grace period may negatively impact traders who in good faith acquired positions that are above that limit. Requiring immediate compliance would force such traders to liquidate positions in order to be at or below the limit. Accordingly, for the purpose of applying limits on speculative positions in newly-determined SPDCs, the Commission proposes to permit a grace period following the ECM's implementation of position limits applicable to SPDCs for traders with cleared positions in such contracts to become compliant with applicable position limit rules. Traders who hold cleared positions on a net basis in the electronic trading facility's SPDC must be at or below the specified position limit no later than 90 calendar days from the date on which the electronic trading facility implements a position limit, unless a hedge exemption is granted by the electronic trading facility. This grace period applies to both initial and subsequent SPDCs on an ECM, and the ECM should promptly notify traders when it has set position limits. This provision is outlined in the proposed Guidance to Core Principle IV.

Rule 36.3(c)(4) requires that the ECM's submission include specific information designed to permit the Commission to evaluate whether the ECM is indeed in compliance with the core principles. Although there are obvious differences between them, this procedure was modeled on the procedure required of applicants to become designated contract markets.<sup>48</sup> As with other aspects of this rulemaking, the Commission is striving to make the procedures and requirements for ECMs with SPDCs as close as possible to those for DCMs, and in this regard will review the adequacy of submitted materials with the same

rigor it applies to DCM applications. Submissions that are incomplete or do not adequately demonstrate compliance with each of the core principles may trigger Commission proceedings under section 5c(d) of the Act and may, pursuant to section 5e or 6 of the Act, result in the revocation of the ECM's right to operate in reliance on the exemption set forth in section 2(h)(3) of the Act with respect to a SPDC.

The Commission also proposes to establish a process for vacating a SPDC determination when the contract no longer meets the criteria specified in section 2(h)(7)(B). Under proposed regulation 36.3(c)(6), the Commission may, on its own initiative or at the request of an ECM with a SPDC, determine that a contract no longer performs a significant price discovery function and vacate its previous determination. Any subsequent determination that the contract once again is a SPDC will be subject to the procedures proposed in regulation 36.3(c)(2). Proposed rule 36.3(c)(6) further provides for the automatic vacation of a significant price discovery contract determination when the SPDC has no open interest and no trading on the contract has occurred for a period of 12 complete calendar months. The Commission is proposing this provision in order to reduce the administrative burden on staff and the compliance burden on an ECM where lack of activity eliminates any possibility that a contract performs a significant price discovery function for the underlying cash market.

#### 4. Substantive Compliance With the Core Principles: Guidance and Acceptable Practices

Section 2(h)(7) of the CEA, as amended, requires that an electronic trading facility on which significant price discovery contracts are traded comply with nine core regulatory principles. Consistent with Congress's intent that status as a registered entity attach to an ECM following the Commission's determination that a particular ECM contract serves a significant price discovery function,<sup>49</sup> these core principles have their origins in their DCM counterparts in section 5 of the CEA and have been construed similarly.<sup>50</sup> The Commission proposes to adopt Appendix B to the part 36 rules to provide general guidance and acceptable practices with respect to compliance with the ECM core principles; the acceptable practices for

compliance with the ECM core principles will, where appropriate, mirror those for DCMs. The Commission intends in the acceptable practices to provide non-exclusive safe harbors for compliance with the core principles by ECMs with SPDCs. As is the case with the core principles established for other registered entities, the guidance offered for ECMs is neither mandatory nor the only means of compliance with the core principles. Consistent with its practice of evaluating a DCM's compliance with the core principles during rule enforcement reviews, the Commission will conduct regular rule enforcement reviews of ECMs with SPDCs to evaluate compliance with the nine core regulatory principles.

The Guidance to *Core Principle I* of section 2(h)(7)(C) of the Act requires the ECM to certify the terms and conditions of the SPDC within 90 calendar days of an ECM's initial SPDC, or 15 calendar days if the ECM has previously traded a SPDC. The acceptable practice for this core principle provides that Guideline No. 1 in Appendix A to the Commission's part 40 rules may be used as guidance to satisfy this provision. To ensure continued compliance with all elements of the Commission's statutory and regulatory regimes for ECMs with SPDCs, the ECM is expected to monitor the SPDC and its trading activity on a continuous basis.

*Core Principle II* requires ECMs to monitor trading in SPDCs to prevent market manipulation and participation abuses. Its guidance and acceptable practices were derived from DCM Core Principle 4 (Monitoring of Trading) and DCM Designation Criterion 2 (Prevention of Market Manipulation).<sup>51</sup> The proposed guidance and acceptable practices in Appendix B to part 36 make clear that ECMs with SPDCs must demonstrate the capacity to prevent market manipulation and have rules deterring trading and participation abuses. Under the proposed guidance, ECMs with SPDCs can demonstrate this capacity through either a dedicated regulatory department or by delegation of that function to an appropriate third party.<sup>52</sup> In either case, the regulatory

<sup>51</sup> 17 CFR 38, Appendices A and B to Part 38.

<sup>52</sup> As is the case for DCMs and DTEFs, ECMs with SPDCs may comply with any core principle through delegation of any relevant function to any registered futures association or another registered entity, but the ECM remains responsible for carrying out the function. Section 5c(b) of the CEA, 7 U.S.C. 7a-2(b). A detailed discussion of registered entities' responsibilities and obligations with respect to delegated functions, as well as a discussion of the distinctions between delegation of functions and outsourcing, or contracting out specified core principle duties is found in the Commission's final rulemaking implementing provisions of the CFMA

<sup>47</sup> Conference Committee Report at 986.

<sup>48</sup> DCM applicants make submissions prior to designation as a registered entity and prior to the listing of any contract, whereas the Commission must review the same information for ECMs after they are deemed registered entities and after the subject contract has established trading volume and open interest.

<sup>49</sup> Conference Committee Report at 986.

<sup>50</sup> 7 U.S.C. 7(d); Conference Committee Report at 985.



department or third party should have an acceptable trade monitoring program, the authority to collect information and documents, and the ability to assess participants' market activity and power.

*Core Principle III* addresses the ability of an ECM with a SPDC to obtain information necessary to perform any of the functions enumerated in section 2(h)(7)(C) of the CEA (the core principles), to provide that information to the Commission, and to have the capacity to carry out any required information sharing agreements. Core Principle III's guidance and acceptable practices have as their source the guidance and acceptable practices of DCM Designation Criterion 8—Ability to Obtain Information.<sup>53</sup> Proposed Appendix B to part 36 makes clear that ECMs with SPDCs must have the authority to collect information and documents on both a routine and non-routine basis; maintain and properly store audit trail data; maintain records in a form and manner acceptable to the Commission; and have the capacity to carry out appropriate information-sharing agreements. In providing guidance on compliance with this requirement, the Commission also proposes to incorporate the guidance and acceptable practices provided for DCM Core Principles 10 (Trade Information) and 17 (Recordkeeping).<sup>54</sup> The Commission believes that the acceptable practices outlined in Core Principle 10 should be made applicable to ECMs with SPDCs because the ability to record full data entry and trade details, as well as the safe storage of audit trail data, is a necessary component in assessing potential manipulation and conducting effective market surveillance. DCM Core Principle 17 requires that DCMs maintain required records in a form and manner acceptable to the Commission and establishes as guidance for acceptable recordkeeping the standards prescribed in Commission regulation 1.31.<sup>55</sup> To ensure that all information required by the Commission is maintained in a uniform manner, the Commission proposes in the acceptable practices for Core Principle III to adopt the acceptable practices for recordkeeping found in DCM Core Principle 17.

*Core Principle IV* requires electronic trading facilities with significant price discovery contracts to establish position

relating to trading facilities ("A New Regulatory Framework"), 66 FR 42256, 42266 (August 10, 2001).

<sup>53</sup> 17 CFR 38, Appendix B to Part 38.

<sup>54</sup> 17 CFR 38, Appendix B to Part 38.

<sup>55</sup> 17 CFR 1.31.

limit or accountability rules for traders in such significant price discovery contracts. Speculative position limits are necessary to reduce the potential for market manipulation. The acceptable practices for Core Principle IV were derived largely from Core Principle 5 for designated contract markets.<sup>56</sup>

DCMs can list for trading futures contracts on a wide range of commodities, including enumerated agricultural products, excluded commodities (e.g., financial products such as currencies), and exempt commodities (e.g., metals, crude oil, natural gas and electricity). Some of these commodities have limited deliverable supplies while others have deep and liquid cash markets. Depending on the variety of possible contracts listed for trading, a DCM may have a mix of position limit and accountability rules. Specifically, futures contracts based on commodities with limited deliverable supplies should have spot-month speculative position limits. In contrast, financial products having deep and liquid cash markets may be eligible for position accountability levels in lieu of position limits since the potential for market manipulation is minimal.

Unlike DCMs, ECMs relying on the exemption in section 2(h)(3) of the CEA are permitted to offer for trading only contracts on exempt commodities. Because the deliverable supplies of exempt commodities typically are limited, the Commission believes that it will be necessary for SPDCs to have spot-month position limits.

The acceptable practices for Core Principle IV make recommendations with respect to how ECMs should establish spot-month speculative position limits. For a unique SPDC,<sup>57</sup> the spot-month speculative position limit should be set in the same manner outlined for contracts listed for trading on DCMs. In this regard, for a physically-delivered SPDC, the level of the spot-month limit should be based upon an analysis of the deliverable supply and the history of spot-month liquidations. The spot-month limit for a physical-delivery market is appropriately set at no more than 25 percent of the estimated deliverable supply.<sup>58</sup> Where a SPDC has a cash

<sup>56</sup> 17 CFR 38, Appendix B to Part 38.

<sup>57</sup> A unique SPDC is one that is not economically equivalent to another SPDC or to a contract traded on a DCM or DTEF.

<sup>58</sup> The Commission notes that deliverable supply typically is less than total supply. In this regard, it is common for some portion of the supply to be unavailable for delivery for a variety of reasons. Deliverable supply is the amount of the underlying commodity that reasonably can be expected to be

settlement provision, the spot-month speculative position limit should be set at a level that minimizes the potential for price manipulation or distortion in the SPDC itself; in related futures and option contracts traded on a DCM or DTEF; in other SPDCs; in other fungible agreements, contracts and transactions; and in the underlying commodity.

The Commission notes that some SPDCs may not be unique. In other words, a SPDC may be economically equivalent to another SPDC or to a contract traded on a DCM or DTEF. Economic equivalence can arise due to substantial similarity among contracts' terms and conditions (e.g., two physically-delivered contracts or two cash-settled contracts having the same specifications). A SPDC also can be economically equivalent to another SPDC or to a contract listed for trading on a DCM or DTEF if it is cash settled based on a daily settlement price or the final settlement price of the referenced contract. For economically-equivalent SPDCs, the electronic trading facility should establish the same spot-month speculative position limits as specified for the equivalent contract.<sup>59</sup>

ECMs should establish non-spot individual month position accountability levels and all-months-combined position accountability levels for its SPDCs. Once a trader exceeds an established position accountability level, the ECM should initiate an investigation to determine whether the individual's trading activity is justified and is not intended to manipulate the market. As part of its investigation, the ECM should inquire about the trader's rationale for holding a net position in excess of the accountability levels. The ECM also can request that the trader not further increase contract positions. If a trader fails to comply with a request for information, provides information that does not sufficiently justify the position, or continues to increase contract positions after a request not to do so is issued by the ECM, then the accountability provisions should enable the ECM to order the trader to reduce the positions.

If a SPDC is economically equivalent to another SPDC or to a contract traded

available to short traders and salable by long traders at its market value in normal cash market channels.

<sup>59</sup> Many DCMs have non-spot individual month and all-months-combined position accountability rules for their futures contracts. Moreover, some DCMs establish non-spot individual month and all-months-combined position limits in lieu of the position accountability levels. The Commission believes that the implementation of such accountability provisions or position limits is a good practice. Accordingly, the Commission proposes to adopt it as an acceptable practice for ECMs.

on a DCM or DTEF, then the ECM should set the non-spot individual month position accountability level and all-months-combined position accountability level at the same level as those specified for the economically-equivalent contract. For a unique SPDC, the ECM should adopt non-spot individual month and all-months-combined position accountability levels that are no greater than 10 percent of the average combined futures and delta-adjusted option month-end open interest for the most recent calendar year.

Position accountability levels are not necessary for SPDCs that specify non-spot individual month position limits and all-months-combined position limits. If a SPDC is economically equivalent to another contract, then the non-spot individual month position limit and all-months-combined position limit should be set at the same levels specified for the equivalent or referenced contract. For unique SPDCs, the non-spot individual month and all-months-combined position limits should be set in the same manner as for position accountability levels, *i.e.*, levels that capture a material amount of large positions that could threaten the market.

An ECM with a SPDC may require that all transactions in that contract be cleared only through a DCO. Alternatively, an ECM's SPDC may not be subject to any clearing requirement, in which case the contract would trade on an uncleared basis. Lastly, an ECM may permit a given SPDC to trade on either a cleared or uncleared basis depending on the status of the counterparties involved. The amendments to the CEA give electronic trading facilities reasonable discretion to take into account the differences between cleared and uncleared transactions when complying with Core Principle IV.<sup>60</sup> For the purpose of applying speculative limits to positions in SPDCs, the ECM should apply speculative position limits to cleared positions only.

Uncleared transactions in SPDCs potentially play an important role in risk management strategies and price formation. As a result, the Commission believes that an ECM should monitor not only trading in cleared transactions but also trading with respect to uncleared transactions. However, the Commission is cognizant of the fact that uncleared trades conducted on the ECM may be offset by trades done off the facility. Such offsetting transactions consummated outside of an ECM

typically are not reported to the facility. Thus, the ECM likely would find it difficult to net uncleared transactions and maintain records of traders' uncleared positions in a given SPDC. In order to account for this situation, the Commission proposes for ECMs with SPDCs a new measure of trading activity called the volume accountability level. For this measure, the ECM should keep track of each trader's uncleared transactions in a SPDC on a net basis that are conducted on the facility. (For the purpose of netting uncleared transactions, long and short uncleared transactions are only offset if they are conducted with the same counterparty.) A volume accountability level is similar to a position accountability level in that a trader may exceed the volume accountability level. However, if a trader's net volume of uncleared trades exceeds the volume accountability level, the ECM should initiate an investigation to determine whether the trading activity is justified and is not intended to manipulate the market. As part of its investigation, the ECM should inquire about the trader's rationale for holding a net volume of uncleared trades in excess of the volume accountability level. The ECM also can request that the trader not further increase the volume of uncleared trades. If a trader fails to comply with a request for information about the portfolio of uncleared trades, provides information that does not sufficiently justify the uncleared transactions conducted, or continues to increase the volume of uncleared trades after a request not to do so is issued by the ECM, then the volume accountability provisions should enable the ECM to require the trader to reduce the volume of uncleared trades.

Consistent with the specific directive of Core Principle IV, the Commission expects ECMs to impose position limit and position accountability requirements on SPDCs as well as positions in agreements, contracts and transactions that are fungible and cleared together with any SPDC. This circumstance typically occurs where an ECM lists a particular contract on its multilateral trading platform and the resultant positions are cleared by a DCO. Separately, the ECM also provides a non-multilateral trading platform capability for the trading of the same contract and the resultant positions are cleared at the same clearing organization together with positions established on the multilateral platform. Given the fact that such arrangements allow market participants to put on positions on the multilateral platform and take them off away from the

platform—as well as vice versa—the Commission believes that it is appropriate for position limit requirements to be applied to overall positions regardless of where they originated.

With regard to compliance with a particular position limit or position accountability rule, ECMs should aggregate on a net basis cleared transactions, including those that are treated by a DCO (registered or unregistered) as fungible with the SPDC. Aggregate positions then will be compared with the applicable position limit and position accountability rules to determine compliance. Uncleared transactions also should be aggregated by trader on a net basis in order to determine whether such trader's volume of uncleared trades exceeds the spot-month volume accountability level.

An ECM with SPDCs should use an automated means of detecting traders' violations of speculative limit rules and exemptions. An automated system also should be used to determine whether a trader has exceeded applicable non-spot individual month accountability levels, all-months-combined accountability levels, and spot-month volume accountability levels. An electronic trading facility should establish a program for effective enforcement of position limits for SPDCs. Lastly, ECMs should use a large trader reporting system to monitor and enforce daily compliance with position limit rules.

The Commission recognizes that some traders with relatively large positions may be adversely affected by newly imposed position limits when a SPDC initially comes into compliance with the core principles. To address this issue, the Commission proposes, for the purpose of applying limits on speculative positions in newly-determined SPDCs, to permit a grace period following issuance of its order for traders with cleared positions in such contracts to become compliant with applicable position limit rules. Traders who hold cleared positions on a net basis in the ECMs SPDC must be at or below the specified position limit level no later than 90 calendar days from the date of the ECM's implementation of position limit rules, unless a hedge exemption is granted by the ECM.

*Core Principle V* requires the ECM to adopt rules to provide for the exercise of emergency authority. The proposed guidance contained in Appendix B to part 36 is substantially similar to the guidance for DCM Core Principle 6.<sup>61</sup> However, the Commission added a

<sup>60</sup> Public Law 110-246 at sec. 13201.

<sup>61</sup> 17 CFR 38, Appendix B to Part 38.

reference in the proposed guidance for Core Principle V to acknowledge that calls for additional margin apply only to contracts that are cleared through a clearinghouse, since not all contracts traded on electronic trading facilities are cleared.

*Core Principle VI* requires that an ECM with a SPDC make public daily information on price, trading volume, and other trading data. The Commission believes this information should include settlement prices, price range, volume, open interest, and other related market information, and has proposed in the acceptable practices that compliance with Commission regulation 16.01,<sup>62</sup> which the Commission proposes to make mandatory for ECMs with SPDCs, would constitute an acceptable practice under Core Principle VI.

*Core Principle VII* requires the ECM to monitor and enforce compliance with the rules of its market. The proposed guidance and acceptable practices provided in Appendix B to part 36 are roughly parallel to the guidance and acceptable practices prescribed for DCM Core Principle 2.<sup>63</sup> The Commission notes that ECMs on which SPDCs are traded are non-intermediated markets, and for this reason guidance relating to a DCM's authority to examine the books and records of intermediaries has not been included in the proposed guidance for Core Principle VII.

*Core Principle VIII* requires the electronic trading facility to establish and enforce rules to minimize conflicts of interest in its decision-making processes. The Commission notes that an ECM may face conflicts between its self-regulatory responsibilities and its commercial interests similar to those encountered by a DCM. For this reason the Commission proposes to insert certain general elements of the acceptable practices for DCM Core Principle 15<sup>64</sup>—specifically, those descriptive elements that provide greater clarity and context to particular conflicts—into paragraph (a)(2) of the guidance section for ECM Core Principle VIII.

The acceptable practices for DCM Core Principle 15 include four specific provisions that must be met to receive the benefit of the safe harbor. These provisions address: (1) Board Composition; (2) Definition of Public Director; (3) Regulatory Oversight Committee; and (4) Disciplinary Panels. Although the Commission did not propose any acceptable practices for Core Principle VIII, the Commission

emphasizes that the four provisions in the acceptable practices for DCM Core Principle 15 are a clear articulation of acceptable methods for managing conflicts of interest in decision-making. Accordingly, the Commission encourages ECMs with SPDCs to consult the DCM Core Principle 15 acceptable practices for additional guidance as to the spirit of Core Principle VIII.

The Commission recognizes that an electronic trading facility may become subject to compliance with Core Principle VIII by virtue of a single contract representing a small portion of the facility's operations. Thus, the ECM's conflicts may be contract-specific and not require the all-encompassing safe harbor offered for the benefit of DCMs in Core Principle 15.<sup>65</sup> The Commission also recognizes that it may not be practicable for an ECM to implement the full panoply of the Core Principle 15 acceptable practices. The ECM must nonetheless ensure that appropriate measures are in place to guard against conflicts of interest in decision-making. An electronic trading facility should carefully consider its method of compliance, including whether additional measures may be required as the number or importance of its SPDCs increases. The Commission reserves the right to issue additional guidance or specific acceptable practices for Core Principle VIII as circumstances warrant.

*Core Principle IX* requires ECMs with SPDCs to avoid adopting rules or taking actions that result in unreasonable restraints of trade or impose a material anticompetitive burden on trading. The Commission is required by section 15(b) of its statute to take into consideration the public interest to be protected by the antitrust laws and to take the least anticompetitive means of achieving the objectives, policies and purposes of the CEA.<sup>66</sup> Consistent with the Commission's approach to antitrust considerations with respect to DCMs,<sup>67</sup> it is the Commission's intent to be guided by section 15(b) of the Act in its consideration of any issues arising under this core principle.

<sup>65</sup> The Commission recognizes that, pursuant to the Reauthorization Act, compliance with the core regulatory principles is limited to ECMs with SPDCs. However, the Commission also recognizes that all ECMs, not just ECMs with SPDCs, may face potential conflicts of interest in their decision-making processes. Therefore, all ECMs may want to consider implementing appropriate measures to minimize conflicts of interests.

<sup>66</sup> 7 U.S.C. 19.

<sup>67</sup> 17 CFR 38, Appendix B to part 38, Guidance for Core Principle 18.

## 5. Annual Commission Review

In accordance with section 2(h)(7) of the CEA, proposed regulation 36.3(d) provides that the Commission will review at least annually agreements, contracts and transactions traded on ECMs to determine whether they serve a significant price discovery function. The Commission proposes to limit these annual reviews to those contracts that have an average daily volume of five or more trades or that have been brought to the attention of the Commission, through the notification procedures of proposed regulation 36.3(c)(2) or otherwise, as possible SPDCs. The Commission believes this approach is consistent with Congress' intent as reflected in the Conference Committee Report:

The Managers do not intend that the Commission conduct an exhaustive annual examination of every contract traded on an electronic trading facility pursuant to the section 2(h)(3) exemption, but instead to concentrate on those contracts that are most likely to meet the criteria for performing a significant price discovery function.<sup>68</sup>

### *B. Market, Transaction and Large Trader Reporting Rules*

The Commission's market and large trader reporting rules ("reporting rules") are contained in parts 15 through 21 of the Commission's regulations.<sup>69</sup> Collectively, the reporting rules effectuate the Commission's market and financial surveillance programs.<sup>70</sup> The market surveillance programs analyze market data to detect and prevent market manipulation and disruptions and to enforce speculative position limits. The financial surveillance programs use market data to measure the financial risks that large contract positions may pose to Commission registrants and clearing organizations.

The Commission's reporting rules can be applied to SPDCs traded on ECMs pursuant to the authority of sections 4a, 4c(b), 4g and 4i of the CEA.<sup>71</sup> The amendments introduced to the CEA by the Reauthorization Act, both by defining ECMs with SPDCs as registered entities with respect to those contracts and by making certain provisions of the

<sup>68</sup> Conference Committee Report at 985.

<sup>69</sup> 17 CFR parts 15 to 21.

<sup>70</sup> See 69 FR 76392 (Dec. 21, 2004).

<sup>71</sup> The Reauthorization Act amended section 2(h)(4)(B) of the Act to subject SPDCs requiring large trader reporting to the provisions of section 4c(b) of the Act. In addition, section 2(h)(4)(D) of the Act provides that transactions executed on ECMs shall be subject to "such rules, regulations, and orders as the Commission may issue to ensure timely compliance with any of the provisions of this Act applicable to a significant price discovery contract traded on or executed on any electronic trading facility \* \* \*." 7 U.S.C. 2(h)(4)(D).

<sup>62</sup> 17 CFR 16.01.

<sup>63</sup> 17 CFR 38, Appendix B to part 38.

<sup>64</sup> *Id.*

Act directly applicable to SPDCs, give the Commission the authority to establish a comprehensive transaction and position reporting system for SPDCs. Specifically, section 4a of the CEA permits the Commission to set, approve exchange-set, and enforce speculative position limits.<sup>72</sup> Section 4c(b) of the Act,<sup>73</sup> which gives the Commission plenary authority to establish the rules pursuant to which the terms and conditions on which commodity options transactions may be conducted, provides the basis for the Commission's authority to establish a large trader reporting system for transactions on ECMs that involve commodity options. Section 4g of the Act, as amended, imposes reporting and recordkeeping obligations on registered persons and requires them to file such reports as the Commission may require on proprietary and customer positions executed on any board of trade and in any SPDC traded or executed on an electronic trading facility.<sup>74</sup> Finally, section 4i of the Act requires the filing of such reports as the Commission may require when positions made or obtained on DCMs, DTEFs or ECMs with respect to SPDCs equal or exceed Commission-set levels.<sup>75</sup>

In addition to proposing technical and conforming amendments to parts 15 through 21 of its regulations, the Commission seeks, through the proposed regulations, to extend to SPDCs the reporting rules that currently apply to DCMs and DTEFs by defining clearing member and clearing organization and amending the definition of reporting market in Commission regulation 15.00 to apply to positions in, and the trading and clearing of, SPDCs executed on ECMs. Under the proposed rules, ECMs would provide clearing member reports for SPDCs to the Commission pursuant to Commission regulation 16.00. As with DCMs, proposed rule 16.01 would require ECMs to submit to the Commission and publicly disseminate option deltas and aggregated trading data on a daily basis.<sup>76</sup> ECM clearing members that clear SPDCs, regardless of their registration status with the Commission or their status as domestic or foreign persons, would be required to

file position reports with the Commission for large SPDC positions held in accounts carried by such brokers when customer positions exceed the contract reporting levels of Commission regulation 15.03(b). In addition, the proposed regulations would require clearing members to identify the owners of reportable SPDC positions on Form 102 (Identification of Special Accounts).<sup>77</sup>

Under the proposed regulations, SPDC traders likewise would be subject to the special call provisions of part 18 of the Commission's regulations for reportable positions. Moreover, clearing members for SPDCs, SPDC traders, and ECMs listing SPDCs each would be subject to the special call provisions of part 21 of the Commission's regulations, which establish the Commission's ability to request information on persons that exercise trading control over commodity futures and options accounts along with additional account-related information for positions that may or may not be reportable under Commission regulation 15.03(b).<sup>78</sup>

In order to effectively communicate with foreign clearing members and foreign traders and to properly administer the proposed special call provisions of parts 17, 18 and 21 of the Commission's regulations, the Commission is also proposing to amend the designation of agent provisions of Commission regulation 15.05. This rule relates to the appointment of an agent for service of process for foreign persons; it is self-effectuating and is designed to permit the Commission to communicate expeditiously with foreign individuals and entities that trade on domestic commodity exchanges.<sup>79</sup> Similar to requirements that currently apply to DCMs and DTEFs, the proposed amendments to regulation 15.05 would require ECMs that list SPDCs to act as the agent of foreign clearing members and foreign traders for

the purpose of accepting service or delivery of any communication, including special calls, issued by the Commission to a foreign clearing member or foreign trader.<sup>80</sup>

The Commission is also proposing new regulation 16.02 to require all reporting markets—a definition that currently includes DCMs and DTEFs (unless the Commission determines otherwise) and, as proposed, will include ECMs listing SPDCs with respect to such contracts—to report on a daily basis trade data and related order information for each transaction that is executed on the market. Such reports would include time and sales data, reference files and such other information as the Commission or its designee may require and, upon request, would be accompanied by data that identifies or facilitates the identification of each trader for each transaction or order included in a submitted report. For some time, DCMs have consistently provided transaction level data to the Commission pursuant to rule 38.5(a), under which they must file trade data upon request by the Commission.<sup>81</sup> Recent acquisitions of technology have enabled the Commission more effectively to integrate trade data and related order information into its trade practice, market and financial surveillance programs. Accordingly, the Commission proposes in new regulation 16.02 to make the submission of trade data and related order information mandatory.

In this regard, and specifically with respect to SPDCs, the Commission notes that the proposed amendments to part 17 of the Commission's regulations do not apply to SPDC transactions that are not cleared for the simple reason that no clearing members are involved in clearing such transactions. For purposes of enforcing SPDC position limits and monitoring large SPDC positions, the Commission would use proposed regulation 16.02 to access transaction information and trader identifications to enforce position limits and monitor large positions for market and financial surveillance purposes.

<sup>77</sup> The Commission's Division of Market Oversight increasingly has been charged with administering the procedural requirements of the reporting rules. Accordingly, the Commission is proposing to shift any delegation of the Commission's authority to determine the format of reports and the manner of reporting under parts 15 through 21 of the Commission's regulations from the Executive Director to the Director of the Division of Market Oversight.

<sup>78</sup> 17 CFR 15.03(b). The proposed rules also seek to amend paragraphs (i)(1) and (i)(2) of Commission regulation 21.01 to ensure that any special call to an intermediary for information that classifies a trader as a commercial or noncommercial trader, and the positions of the trader as speculative, spread positions, or positions held to hedge commercial risks, can be made with respect to both commodity futures and commodity options contracts. 17 CFR 21.02(i).

<sup>79</sup> For background on the adoption of the rule, *see* 45 FR 30426 (May 8, 1980).

<sup>80</sup> In order to ensure that the Commission can expeditiously communicate with all foreign individuals and entities that may effect transactions in ECM SPDCs, the Commission is proposing to define the term foreign clearing member in proposed regulation 15.00(g), and to use that term along with the term foreign trader as defined in regulation 15.00(h), in proposed regulation 15.05(i).

<sup>81</sup> 17 CFR 38.5(a).

<sup>72</sup> 7 U.S.C. 6a.

<sup>73</sup> 7 U.S.C. 6c(b).

<sup>74</sup> 7 U.S.C. 6g.

<sup>75</sup> 7 U.S.C. 6i.

<sup>76</sup> Currently, the public dissemination requirement of Commission regulation 16.01(e) applies only to DCMs. The proposed rules would uniformly apply the public dissemination requirement of Commission regulation 16.01(e) to actively traded DCM contracts and SPDCs executed on DTEFs and ECMs. 17 CFR 16.01(e).

### C. Other Regulatory Provisions

#### 1. Part 40—Provisions Common to Registered Entities

ECMs with SPDCs are integrated into the definition of “registered entity” in section 1a(29) of the CEA, as amended. Part 40 of the Commission’s regulations applies to registered entities, and therefore, ECMs with SPDCs. Proposed part 40 is being amended to specify which provisions would be, or would not be, applicable to all registered entities. In particular, rules 40.1, 40.2 and 40.5–40.8 and Appendix D apply to ECMs with SPDCs. Although not all provisions of part 40 will be applicable to ECMs with SPDCs,<sup>82</sup> interested parties are strongly encouraged to review all of part 40 because even those sections that are not being amended in this rulemaking may be *de facto* amended by virtue of the fact that the term “registered entity” now includes ECMs with SPDCs.

### III. Related Matters

#### A. Cost Benefit Analysis

Section 15(a) of the Act requires the Commission to consider the costs and benefits of its actions before issuing new regulations under the Act. Section 15(a) does not require the Commission to quantify the costs and benefits of new regulations or to determine whether the benefits of adopted regulations outweigh their costs. Rather, section 15(a) requires the Commission to consider the cost and benefits of the subject regulations. Section 15(a) further specifies that the costs and benefits of the regulations shall be evaluated in light of five broad areas of market and public concern: (1) Protection of market participants and the public; (2) efficiency, competitiveness, and financial integrity of the market for listed derivatives; (3) price discovery; (4) sound risk management practices; and (5) other public interest considerations. The Commission may, in its discretion, give greater weight to any one of the five enumerated areas of concern and may, in its discretion, determine that, notwithstanding its costs, a particular regulation is 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 regulations implement the Reauthorization Act by establishing an enhanced level of oversight of

ECMs—including ECMs with SPDCs and ECM market participants—as mandated by Reauthorization Act. As a result, in certain cases, it may be more appropriate to attribute the compliance costs imposed by the proposed regulations to requirements that directly arise from the provisions of the Reauthorization Act.

Under the proposed rules, all DCMs, DTEFs (unless the Commission determines otherwise) and ECMs with SPDCs would be required to provide daily transaction and related data reports to the Commission under proposed rule 16.02. The costs associated with the daily transaction and related data reporting requirements of proposed regulation 16.02, however, may be ameliorated by the fact that DCMs have been voluntarily providing transactional data to the Commission on a daily basis since the mid-1980s. The Commission estimates that DCMs would account for the substantial majority of the markets that would likely be required to file such reports pursuant to proposed rule 16.02.

The proposed regulations would extend the market and position reporting requirements of parts 15 to 21 of the Commission’s regulations to ECMs with SPDCs with respect to such contracts. The requirements of the proposed regulations are substantial, would involve the submission of daily reports, and would impose burdens on market participants that clear and trade SPDCs. More specifically, the proposed rules would require ECMs with SPDCs with respect to such contracts to provide clearing member reports for SPDCs to the Commission pursuant to Commission regulation 16.00. Proposed rule 16.01 would require ECMs to submit to the Commission and publicly disseminate option deltas and aggregated trading data on a daily basis. Pursuant to proposed rule 17.00 ECM clearing members that clear SPDCs would be required to file position reports with the Commission for large SPDC positions held in accounts carried by such brokers when customer positions exceed contract reporting levels and would be required to identify the owners of reportable SPDC positions on Form 102 under proposed rule 17.01. SPDC traders likewise would be subject to the special call provisions of part 18 of the Commission’s regulations for reportable positions, and clearing members for SPDCs, SPDC traders, and ECMs listing SPDCs each would be subject to the special call provisions of part 21 of the Commission’s regulations.

The costs associated with the requirements of the market and position reporting rules, should, however, be

reduced in part by the substantial overlap between the persons that are currently subject to the reporting rules, and the persons that would be subject to the reporting rules pursuant to the Commission’s proposed regulations. For example, there is substantial overlap between traders of the natural gas contract on ICE OTC and traders of the same contract on NYMEX. With respect to clearing members of ICE OTC, for example, such persons are often clearing members or affiliates of clearing members of NYMEX.

The benefits of extending the market and reporting rules to SPDCs are substantial. As an initial matter, it is important to note that a significant focus of the Reauthorization Act concerned amending the CEA with the specific intent of giving the Commission the authority to extend the market and position reporting rules to SPDC markets and market participants. To the extent that contracts listed on ECMs serve a significant price discovery function, the regulatory value of enhanced oversight, through the application of the market and position reporting rules to such contracts, is elevated. The Commission analyzes the information funneled to it by the requirements of the market and position reporting rules to conduct market and financial surveillance. Without such information, the ability of the Commission to discharge its regulatory responsibilities, including the responsibilities of preventing market manipulations and contract price distortions and ensuring the financial integrity of the listed derivatives marketplace, would be compromised.

The bulk of the costs that would be imposed by the requirements of proposed regulation 36.3 relate to significant and increased submission of information requirements. For example, under proposed regulation 36.3(b)(1), all ECMs would be required to file certain basic information including contract terms and conditions with, and make certain demonstrations related to compliance with the terms of the section 2(h)(3) exemption to, the Commission. Proposed regulation 36.3(b)(2) would require ECMs to submit transactional information on a weekly basis to the Commission for certain traded contracts that are not SPDCs and would not be subject to the terms of proposed rule 16.02. Proposed regulation 36.3(c)(4) would impose a substantial cost on ECMs with SPDCs in terms of providing information to the Commission.

In enacting the Reauthorization Act, Congress directed the Commission to take an active role in determining

<sup>82</sup> Regulation 40.3 will not apply to ECMs with SPDCs because it addresses Commission approval of products. Regulation 40.4 applies solely to agricultural products, which cannot be traded on ECMs.

whether contracts listed by ECMs could qualify as SPDCs. Accordingly, the enhanced informational requirements that would be imposed on ECMs with respect to contracts that have not been identified as SPDCs have been proposed by the Commission in order to acquire the information that it requires to discharge this newly mandated responsibility. In addition, the substantial information submission and demonstration requirements that would be imposed on ECMs with SPDCs have been proposed because ECMs with SPDCs, by statute, acquire certain of the self-regulatory responsibilities of DCMs. The submission requirements associated with proposed regulation 36.3(c)(4) are tailored to enable the Commission to ensure that ECMs with SPDCs, as entities with the elevated status of a registered entity under the Act, are in compliance with the statutory terms of the core principles of section 2(h)(7)(C) of the Act. As with the market and position reporting rules, the primary benefit to the public of proposed regulation 36.3 is that its requirements give the Commission the ability to discharge its statutorily mandated responsibility for monitoring for the presence of SPDCs and extending its oversight to the trading of SPDCs.

#### 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, 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>83</sup> Similarly, clearing members, foreign brokers and traders would be subject to the proposed regulations only if carrying or holding large positions. Accordingly, the Acting Chairman, on behalf of the Commission, hereby certifies, pursuant to 5 U.S.C. 605(b), that the actions proposed to be taken herein will not have a significant economic impact on a substantial number of small entities.

#### C. Paperwork Reduction Act

Certain provisions of proposed Commission regulation 36.3 would result in new collection of information requirements within the meaning of the Paperwork Reduction Act of 1995

(PRA).<sup>84</sup> The Commission therefore is submitting this proposal to the Office of Management and Budget (OMB) for review in accordance with 44 U.S.C. 3507(d) and 5 CFR 1320.11. The title for this collection of information is “Regulation 36.3—Exempt Commercial Market Submission Requirements” (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, “Commission Records and Information.” In addition, 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>85</sup>

The requirements of Commission regulation 36.3 are currently covered by OMB control number 3038–0054 which applies to both EBOTs and ECMs. As a result of the Reauthorization Act, EBOTs and ECMs have to comply with additional divergent regulatory requirements. Accordingly, the Commission is seeking a new and separate control number for ECMs operating in compliance with the requirements of regulation 36.3. Upon OMB’s approval and assignment of a separate control number specifically for the collection of information requirements of proposed regulation 36.3, the Commission intends to submit the necessary documentation to OMB to enable it to apply OMB control number 3038–0054 exclusively to EBOTs.

In addition, the Commission is proposing amendments to parts 15 to 21 of the Commission’s regulations, which amend two existing collections of information titled “Large Trader Reports” (OMB control number 3038–0009) and “Futures Volume, Open Interest, Price, Deliveries, and Exchanges of Futures” (OMB control number 3038–0012). Responses to this collections of information would be mandatory. Where appropriate, the Commission will protect proprietary information pursuant to the Freedom of Information Act<sup>86</sup> and 17 CFR part 145, “Commission Records and Information.” In addition, section 8(a)(1) of the Act 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>87</sup>

Finally, proposed regulation 16.02 would result in a new collection of information requirement within the meaning of the PRA. The Commission is therefore submitting the proposal for regulation 16.02 to OMB for review. The title for the collection of information requirement is “Regulation 16.02—Daily Trade and Supporting Data Reports” (OMB control number 3038–NEW). If adopted, this collection would be mandatory. The Commission will protect proprietary information according to the Freedom of Information Act and 17 CFR part 145, “Commission Records and Information.” In addition, 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>88</sup>

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. OMB has not yet assigned control numbers to the new collections for proposed regulations 36.3 and 16.02. The approved collection of information requirements associated with parts 15 to 21, which would be revised by the proposed rules and rule amendments, display control numbers 3038–0009 and 3038–0012.

#### 1. Proposed Regulation 36.3

##### A. Regulation 36.3(a)

Regulation 36.3(a) requires that ECMs notify the Commission of the intent to operate as an ECM in reliance of section 2(h)(3) of the Act and further provide the information and certifications required by section 2(h)(5)(A) of the Act. Section 2(h)(5)(A) of the Act requires an ECM to provide the name and address of the person who is authorized on behalf of the ECM to receive communications from the Commission, the commodity categories that the ECM intends to offer, and certifications that certain owners and principals of the ECM are not bad actors, that the facility will comply with the requirements of the ECM exemption, and that the facility will update its filings under section 2(h)(5)(A) to account for material changes in the information submitted to the Commission.

<sup>84</sup> 44 U.S.C. 3501–3520.

<sup>85</sup> 7 U.S.C. 12(a)(1).

<sup>86</sup> 5 U.S.C. 552 *et seq.*

<sup>87</sup> *Id.*

<sup>88</sup> *Id.*

<sup>83</sup> 47 FR 18618 (April 30, 1982).

The substantive requirements of regulation 36.3(a) repeat the requirements that are imposed by the Act as a condition of operating pursuant to the ECM exemption. The reporting or recordkeeping burden associated with Commission regulation 36.3(a) involves the compilation and submission of the required information to the Commission. Commission staff estimates that each ECM would expend approximately 4 hours of professional time annually to maintain, verify, and update the notification and required certifications. Commission staff estimates that 20 ECMs will be subject to the requirement resulting in an aggregate burden of 80 hours annually.

#### B. Regulation 36.3(b)(1)

Under proposed regulation 36.3(b)(1), each ECM would be required to provide contract descriptions and terms and conditions, the market's trading conventions, and the market's trading protocols to the Commission. Each ECM would be required to describe how it meets the statutory definition of a trading facility and demonstrate that it requires each participant to comply with all applicable laws; complies with the initial statutory requirements for the ECM exemption under section 2(h)(3) of the Act; and directs a program to monitor market participants for compliance with the transactional requirements of the ECM exemption. Proposed regulation 36.3(b)(1) would further require that each ECM provide, upon the Commission's request, information that the Commission would deem helpful to its determination as to whether a particular contract is a SPDC. Lastly, each ECM would be required to annually indicate on Form 205 whether it continues to operate under the ECM exemption and certify the accuracy of the information contained in its Notification of Operation submitted pursuant to section 2(h)(5)(A) of the Act and regulation 36.3(a).

Based on the number of contract submissions made by DCMs, the Commission estimates that ECMs collectively would list for trading 250 commodity futures and options contracts annually. Commission staff estimates that compliance with the above requirements and the transmission of descriptions and terms and conditions for such products would take approximately 2 hours of professional time to prepare per contract resulting in a collective burden of 500 hours annually for all ECMs.

#### C. Regulation 36.3(b)(2)

Proposed regulation 36.3(b)(2) would require that ECMs, with respect to

contracts that are not SPDCs, identify contracts which average 5 or more trades per day over a calendar quarter, and for such contracts, compile daily transaction-based reports that include the date of execution, the time of execution, the price of execution, the quantity executed, the total daily trading volume, the total open interest, option type, option strike prices for each qualifying contract, and such other information as may be requested by the Commission. Proposed regulation 36.3(b)(2) would require the submission of the reports on a weekly basis. Such data is generated by ECMs in the normal course of operation. The Commission staff estimates that ECMs would submit weekly reports for a total of 40 contracts annually (2,080 reports). Commission staff estimates that ECMs would expend approximately 20 minutes of professional time to compile and transmit each weekly report to the Commission resulting in an annual burden of approximately 693 hours.

Proposed regulation 36.3(b)(2) would give an ECM the flexibility to choose to submit weekly transaction-based reports or, in the alternative, give the Commission electronic access to its trading facility to enable the Commission to create the weekly reports. Should an ECM select this option, Commission staff believes that such access would not result in any estimable burden on an ECM.

Proposed regulation 36.3(b)(2) also would require that ECMs, with respect to contracts that are not SPDCs, to identify contracts which average 1 or more trades per day over a calendar quarter, and for such contracts, to provide to the Commission on a quarterly basis, the terms and conditions of such contracts, the average daily trading volume, and the most recent level of open interest. As with weekly reports, such data is generated by ECMs in the normal course of operation. The Commission staff estimates that ECMs would submit quarterly reports for a total of 90 contracts annually (360 total reports). Commission staff estimates that ECMs would expend approximately 20 minutes of professional time to compile and transmit each quarterly report resulting in an annual burden of 120 hours.

Furthermore, proposed regulation 36.3(b)(2) would require ECMs to maintain an inventory of all fraud or manipulation based complaints and submit a copy of such complaints to the Commission within 3 or 30 days, depending on the specific facts of the complaints. ECMs should record and retain an inventory of complaints in the

normal course of operation. Commission staff is unable to estimate the hourly burden associated with the routine transmittal of such reports to the Commission. However, Commission staff would presume that such transmittal requirements should not result in any materially measurable burden on ECMs.

Lastly, proposed regulation 36.3(b)(2) addresses the Commission's authority to require the submission of data upon special call under section 2(h)(5)(B)(iii) of the Act. Pursuant to that section of the Act, the Commission has the authority to issue special calls in order to enforce certain provisions of the Act including the anti-fraud and anti-manipulation provisions. In addition, the Commission is authorized to issue special calls to ECMs to facilitate its determination as to whether certain contracts are SPDCs, to evaluate a systemic market event, or to obtain information requested by another Federal financial regulator. Commission staff estimates that a total of 15 special calls would be issued to ECMs annually under section 2(h)(5)(B)(iii) of the Act. Each ECM that has been issued a special call would expend approximately 5 hours of professional time to respond to the call resulting in a burden of 75 hours annually.

#### D. Proposed Regulation 36.3(c)(2)

Proposed regulation 36.3(c)(2) establishes for ECMs certain requirements for notifying the Commission of possible SPDCs that may be listed by the ECM. Specifically, an ECM's obligation to notify the Commission would apply to contracts that average 5 trades or more per day over the most recent calendar quarter, and may be triggered by either the ECM's sale of contract price data or by a contract's daily settlement price being within 2.5 percent of the contemporaneously determined closing, settlement or daily price of another contract 95 percent or more of the days in the most recent quarter. Such notifications would be accompanied by supporting details. Commission staff estimates that cost of monitoring for the triggering conditions is nominal. Commission staff estimates that collectively 10 contracts would be the subject of the notification requirement annually. Each ECM with a qualifying contract would expend approximately 1 hour of professional time to compile and transmit such data to the Commission at an aggregate annual burden of 10 hours.



#### E. Proposed Regulation 36.6(c)(4)

An ECM with a SPDC, with respect to such a contract, has substantial regulatory responsibilities including the obligation to comply with the core principles of section 2(h)(7)(C) of the Act and to certify the compliance of SPDC contract terms and conditions and exchange rules with the core principles, other applicable provisions of the Act, and Commission regulations thereunder. To enable the Commission to evaluate an ECM's compliance with the statutory and regulatory provisions applicable to SPDCs and ECMs listing SPDCs, Commission regulation 36.3(c)(4) would require ECMs with SPDCs to submit a substantial amount of information and documentation to the Commission including the market's rules, a description of financial standards for members or participants, a description of the market's trading algorithm, legal status documents, and a description of the governance structure of the market. As proposed, such information collectively would be filed only once upon the market's listing of a SPDC. However, subsequent exchange rule changes, as with initial SPDC contract terms and conditions and amendments thereto, would be required to be certified on an ongoing basis.

Commission staff estimates that up to three new ECMs could list at least one SPDC during the next five years. Commission staff estimates that each new ECM listing its initial SPDC would expend approximately 200 hours of professional time providing the information and documentation required under regulation 36.3(c)(4) for an aggregate burden of 600 hours. Assuming that such trading facilities will operate for ten years, the aggregated annualized cost, in terms of burden hours, would be 60 hours. Additionally, Commission staff estimates that the Commission would receive approximately 50 certified filings per SPDC. For each SPDC related certified filing, an ECM would expend, in accordance with the procedural and submission requirements of Commission regulation 40.6, approximately 30 minutes resulting in an aggregate annual burden of 75 hours.

#### F. Proposed Regulation 36.3(c)(6)

Proposed regulation 36.3(c)(6) requires an ECM listing a SPDC, upon the Commission's request, to file a written demonstration that the ECM is in compliance with the core principles of section 2(h)(7)(C) of the Act. Commission staff estimates that such demonstrations of compliance could require up to 20 hours of response time.

Commission staff anticipates issuing 2 requests annually resulting in an aggregate burden of 40 hours.

#### 2. Proposed Regulation 16.02

Under proposed regulation 16.02, reporting markets, a term which as proposed would include ECMs with SPDCs with respect to SPDCs, in addition to DCMs and DTEFs (unless determined otherwise by the Commission), would be required to provide trade and supporting data reports to the Commission on a daily basis. Such reports would include transaction-level trade data and related order information for each transaction executed on the reporting market and would be accompanied by data that identifies traders for each transaction when reporting markets maintain such data.

Since the mid-1980s, all DCMs have voluntarily provided the Commission with transaction level data on a daily basis. Proposed regulation 16.02 seeks to formalize and codify the submission process. Commission staff estimates that each reporting market would expend 18 hours for onsite visits to the Commission, discussions with staff to introduce the order flow process, and meetings with staff for follow-up discussions. The proposed rules would require that reporting markets expend approximately 2325 hours in additional start-up costs to establish the required information technology infrastructure. Commission staff estimates that it would receive daily trade and supporting data reports from up to 15 reporting markets annually. Accordingly the start-up burden in terms of hours would in the aggregate be 35,145 hours. Annualized over a useful life of ten years, the aggregated annual burden hours would be 3,514.

It is also estimated that start-up and continuing costs may involve product and service purchases. Commission staff estimates that reporting markets could expend up to \$5,000 annually per market on product and service purchases to comply with proposed regulation 16.02. This would result in an aggregated cost of \$75,000 per annum (15 reporting markets × \$5,000). This estimate, however, is speculative because reporting markets must possess the ability to audit and track transactions in the ordinary course of operations independently of proposed regulation 16.02.

In addition to the start-up burden, proposed regulation 16.02, if adopted, would impose certain ongoing costs. Commission staff estimates that each reporting market would expend 30 minutes for each daily trade and

supporting data report transmitted to the Commission resulting in an aggregate burden of 1,875 hours annually (assuming that such reports are provided for each of 250 trading days).

#### 3. Market and Large Trader Reporting Rules

In order to implement the CEA as amended by the Reauthorization Act, the Commission through this rulemaking proposes to extend the market and large trader reporting requirements that currently apply to DCMs and DTEFs to ECMs with SPDCs with respect to such contracts.

#### A. Futures Volume, Open Interest, Price, Deliveries, and Exchanges of Futures (OMB control number 3038-0012)

Twelve exchanges currently submit aggregated market data to the Commission and are required to publicly disseminate for each of approximately 250 trading days per year under Commission regulation 16.01. The information includes aggregate figures on a per contract basis on total gross open contracts, open futures contracts against which delivery notices have been stopped, volume generated from the exchange of futures, delta factors as well as certain pricing data. Should the proposed amendments be adopted, it is estimated that up to 15 reporting markets, including ECMs with SPDCs with respect to such contracts, could be required to submit this data to the Commission on a continuing basis. Commission staff estimates that such markets would expend approximately 30 minutes per day to generate the required data files, transmit that file to Commission offices, and publish the required information. This would result in an annual burden of approximately 1,875 hours.

#### B. Large Trader Reports (OMB Control Number 3038-0009)

##### 1. Clearing Member Reports

Twelve designated contract markets provide clearing member reports pursuant to Commission regulation 16.00 once on each of an estimated 250 trading days per year. Should the proposed rules be adopted, it is estimated that up to 15 reporting markets, including ECMs with SPDCs with respect to such contracts, would be providing this data to the Commission on a continuing basis. The exchanges and ECMs would be required to submit confidential information to the Commission on the aggregate positions and trading activity of each clearing member.

Reporting markets, on a daily basis, are required under regulation 16.00 to

report each clearing member's open long and short positions, purchases and sales, exchanges of futures, and futures delivery notices. The data is reported separately by proprietary and customer accounts by futures month and, for options, by puts and calls by expiration date and strike price. The Commission obtains clearing member reports from the reporting markets or the clearing organizations of each reporting market. Reporting markets and the clearing organizations routinely compile, analyze and provide such data to each clearing member. Since the data is routinely provided to clearing members, the reporting burden for this set of data is estimated at 20 minutes for each reporting market per day. Assuming that a total of 15 entities would provide this data on a daily basis to the Commission, the total aggregate burden hours for reporting would be 1,250 hours (assuming that there are 250 trading days annually).

## 2. Reporting Firms

Under Commission regulation 17.00, routine reports are filed only for accounts with commodity futures and option positions that exceed levels set by the Commission in regulation 15.03(b). As proposed, regulation 17.00 would extend the routine reporting requirements of regulation 17.00 to clearing members on ECMs with SPDCs with respect to SPDCs. Should proposed regulation 17.00 be adopted, it is estimated that up to an additional 30 respondents would be required to file reports at any one time under regulation 17.00 increasing the total number of respondents to 250. The reporting burden consists of staff of reporting firms initializing their information technology systems for new contracts and new accounts. On average it is expected that about 15 minutes per day is expended by these reporting firm staff. Over 250 trading days annually, the aggregate burden would be 15,625 hours.

## 3. Forms 102

Each account reported to the Commission by an FCM, clearing member, or foreign broker must also be identified on a Form 102 pursuant to regulation 17.01. By amending the definition of reporting market, clearing member, and clearing organization, the notice of proposed rulemaking would extend the requirements of regulation 17.01 to clearing members of ECMs with SPDCs with respect to such contracts. Forms 102 provide information that allows the Commission to combine different accounts held or controlled by the same trader and to identify

commercial firms using the markets for hedging. Should the notice of proposed rulemaking be adopted, the total number of Forms 102 filed with the Commission is estimated to increase by 500 to 4,500 per year. Respondents would expend 12 minutes completing each form for a total aggregate burden of 900 hours annually.

## 4. Reports From Traders

Traders provide identifying information using Forms 40 under Commission regulation 18.04 and position data upon special call under Commission regulations 18.00 and 18.05. The notice of proposed rulemaking would extend the requirements of those regulations to traders of SPDCs. Should the proposed amendments be adopted, the total estimated number of traders filing the Form 40 under regulation 18.04 would increase by 100 to 2,500 per year with each response requiring approximately 20 minutes, resulting in an aggregate annual burden of 833 hours.

The Commission has maintained the authority to make special calls on traders under part 18 of the Commission's regulations when the information obtained routinely under part 17 of the Commission's regulations is incomplete for its market and financial surveillance purposes. Information obtained on call under Commission regulations 18.00 and 18.05 is provided in the manner stipulated per instruction contained in the special call. Should the proposed regulations be adopted, the Commission estimates that 12 special calls would be issued to each of 45 traders under Commission regulations 18.00 and 18.05 and that each response to a call would require approximately 5 hours, for an estimated aggregate annual burden of 2,700 hours.

## 5. Part 21 of the Commission Regulations

Under part 21 of the Commission's regulations, the Commission may issue special calls for additional cash and futures data concerning traders from FCMs, introducing broker, clearing members, foreign brokers, and traders. In addition, under part 21 of the Commission's regulations (17 CFR part 21), the Commission may request identifying information regarding persons who exercise trading control over accounts. Position information collected pursuant to special call under part 21 of the Commission's regulations may be used to audit large trader reports and is used to investigate potential market abuses. Although similar to the standardized information routinely collected under part 17 of the

Commission's regulations for reportable accounts, such data is submitted in response to customized requests for information and may regard accounts and positions that are not reportable. In contrast to special calls for identifying data made under Commission regulation 18.04, special calls made under any provision of part 21 of the Commission's regulations generally occur only when a particular market shows a potential for disruption or when there is an investigation of possible violations of the Act or the regulations thereunder. The notice of proposed rulemaking would apply the terms of part 21 to ECMs with SPDCs with respect to such contracts, clearing members clearing SPDCs, and SPDC traders. Should the proposed regulations be adopted, the Commission estimates that the Commission will continue to make less than 10 special calls under all of the provisions of part 21 of the Commission's regulations and that each response to a call will require approximately 1 hour, resulting in an aggregate reporting burden of 10 hours annually.

## 4. Information Collection Comments

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: (i) 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; (ii) evaluate the accuracy of the Commission's estimate of the burden of the proposed collections of information; (iii) determine whether there are ways to enhance the quality, utility, and clarity of the information to be collected; and (iv) 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.

You may submit your comments 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 your comments so that we can summarize all written comments and address them in the final rule preamble. Refer to the Addresses section of this notice of proposed rulemaking for comment submission instructions to the Commission. You may obtain a copy of the supporting statements for the

collections of information discussed above by visiting RegInfo.gov. OMB is required to make a decision concerning the collections of information between 30 and 60 days after publication of this Release. Consequently, a comment to OMB is most assured of being fully effective if received by OMB (and the Commission) within 30 days after publication of this notice of proposed rulemaking.

#### List of Subjects

##### 17 CFR Part 15

Brokers, Commodity futures, Reporting and recordkeeping requirements.

##### 17 CFR Part 16

Commodity futures, Reporting and recordkeeping requirements.

##### 17 CFR Part 17

Brokers, Commodity futures, Reporting and recordkeeping requirements.

##### 17 CFR Part 18

Commodity futures, Reporting and recordkeeping requirements.

##### 17 CFR Part 19

Commodity futures, Cottons, Grains, Reporting and recordkeeping requirements.

##### 17 CFR Part 21

Brokers, Commodity futures, Reporting and recordkeeping requirements.

##### 17 CFR Part 36

Commodity futures, Commodity Futures Trading Commission.

##### 17 CFR Part 40

Commodity futures, Contract markets, Designation application, Reporting and recordkeeping requirements.

For the reasons stated in the preamble, the Commodity Futures Trading Commission proposes to amend 17 CFR parts 15, 16, 17, 18, 19, 21, 36 and 40 as follows:

#### PART 15—REPORTS—GENERAL PROVISIONS

1. The authority citation for part 15 is revised to read as follows:

**Authority:** 7 U.S.C. 2, 5, 6a, 6c, 6f, 6g, 6i, 6k, 6m, 6n, 7, 7a, 9, 12a, 19, and 21, as amended by Title XIII of the Food, Conservation and Energy Act of 2008, Pub. L. No. 110–246, 122 Stat. 1624 (June 18, 2008).

2. Revise § 15.00 to read as follows:

#### § 15.00 Definitions of terms used in parts 15 to 21 of this chapter.

As used in parts 15 to 21 of this chapter:

(a) *Cash or Spot*, when used in connection with any commodity, means the actual commodity as distinguished from a futures or option contract in such commodity.

(b) *Clearing member* means any person who is a member of, or enjoys the privilege of clearing trades in his own name through, the clearing organization of a designated contract market, registered derivatives transaction execution facility, or registered entity under section 1a(29) of the Act.

(c) *Clearing organization* means the person or organization which acts as a medium for clearing transactions in commodities for future delivery or commodity option transactions, or for effecting settlements of contracts for future delivery or commodity option transactions, for and between members of any designated contract market, registered derivatives transaction execution facility or registered entity under section 1a(29) of the Act.

(d) *Compatible data processing media* means data processing media approved by the Commission or its designee.

(e) *Customer* means “customer” (as defined in § 1.3(k) of this chapter) and “option customer” (as defined in § 1.3(jj) of this chapter).

(f) *Customer trading program* means any system of trading offered, sponsored, promoted, managed or in any other way supported by, or affiliated with, a futures commission merchant, an introducing broker, a commodity trading advisor, a commodity pool operator, or other trader, or any of its officers, partners or employees, and which by agreement, recommendations, advice or otherwise, directly or indirectly controls trading done and positions held by any other person. The term includes, but is not limited to, arrangements where a program participant enters into an expressed or implied agreement not obtained from other customers and makes a minimum deposit in excess of that required of other customers for the purpose of receiving specific advice or recommendations which are not made available to other customers. The term includes any program which is of the character of, or is commonly known to the trade as, a managed account, guided account, discretionary account, commodity pool or partnership account.

(g) *Discretionary account* means a commodity futures or commodity option trading account for which buying or selling orders can be placed or

originated, or for which transactions can be effected, under a general authorization and without the specific consent of the customer, whether the general authorization for such orders or transactions is pursuant to a written agreement, power of attorney, or otherwise.

(h) *Exclusively self-cleared contract* means a cleared contract for which no persons, other than a reporting market and its clearing organization, are permitted to accept any money, securities, or property (or extend credit in lieu thereof) to margin, guarantee, or secure any trade.

(i) *Foreign clearing member* means a “clearing member” (as defined by paragraph (b) of this section) who resides or is domiciled outside of the United States, its territories or possessions.

(j) *Foreign trader* means any trader (as defined in paragraph (o) of this section) who resides or is domiciled outside of the United States, its territories or possessions.

(k) *Guided account program* means any customer trading program which limits trading to the purchase or sale of a particular contract for future delivery of a commodity or a particular commodity option that is advised or recommended to the participant in the program.

(l) *Managed account program* means a customer trading program which includes two or more discretionary accounts traded pursuant to a common plan, advice or recommendations.

(m) *Open contracts means* “open contracts” (as defined in § 1.3(t) of this chapter) and commodity option positions held by any person on or subject to the rules of a board of trade which have not expired, been exercised, or offset.

(n) *Reportable position* means:

(1) For reports specified in parts 17, 18 and § 19.00(a)(2) and (a)(3) of this chapter any open contract position that at the close of the market on any business day equals or exceeds the quantity specified in § 15.03 of this part in either:

(i) Any one future of any commodity on any one reporting market, excluding future contracts against which notices of delivery have been stopped by a trader or issued by the clearing organization of a reporting market; or

(ii) Long or short put or call options that exercise into the same future of any commodity, or long or short put or call options for options on physicals that have identical expirations and exercise into the same physical, on any one reporting market.

(2) For the purposes of reports specified in § 19.00(a)(1) of this chapter, any combined futures and futures-equivalent option open contract position as defined in part 150 of this chapter in any one month or in all months combined, either net long or net short in any commodity on any one reporting market, excluding futures positions against which notices of delivery have been stopped by a trader or issued by the clearing organization of a reporting market, which at the close of the market on the last business day of the week exceeds the net quantity limit in spot, single or in all-months fixed in § 150.2 of this chapter for the particular commodity and reporting market.

(o) *Reporting market* means a designated contract market, registered entity under section 1a(29)(E) of the Act, and unless determined otherwise by the Commission with respect to the facility or a specific contract listed by the facility, a registered derivatives transaction execution facility.

(p) *Special account* means any commodity futures or option account in which there is a reportable position.

(q) *Trader* means a person who, for his own account or for an account which he controls, makes transactions in commodity futures or options, or has such transactions made.

3. In § 15.01, revise paragraph (a) to read as follows:

**§ 15.01 Persons required to report.**

\* \* \* \* \*

(a) Reporting markets—as specified in parts 16, 17, and 21 of this chapter.

\* \* \* \* \*

4. In § 15.05, revise the heading and paragraph (a); and add paragraph (i) to read as follows:

**§ 15.05 Designation of agent for foreign persons.**

(a) For purposes of this section, the term “futures contract” means any contract for the purchase or sale of any commodity for future delivery, or a contract identified under § 36.3(b)(i) of this chapter as traded in reliance on the exemption in section 2(h)(3) of the Act, traded or executed on or subject to the rules of any designated contract market or registered derivatives transaction execution facility, or for the purposes of paragraph (i) of this section, a reporting market; the term “option contract” means any contract for the purchase or sale of a commodity option, or as applicable, any other instrument subject to the Act pursuant to section 5a(g) of the Act, traded or executed on or subject to the rules of any designated contract market or registered derivatives transaction execution facility, or for the

purposes of paragraph (i) of this section, a reporting market; the term “customer” means any person for whose benefit a foreign broker makes or causes to be made any futures contract or option contract; and the term “communication” means any summons, complaint, order, subpoena, special call, request for information, or notice, as well as any other written document or correspondence.

\* \* \* \* \*

(i) Any reporting market that is a registered entity under section 1a(29)(E) of the Act that permits a foreign clearing member or foreign trader to clear or effect contracts, agreements or transactions on the trading facility or its clearing organization, shall be deemed to be the agent of the foreign clearing member or foreign trader with respect to any such contracts, agreements or transactions cleared or executed by the foreign clearing member or the foreign trader. Service or delivery of any communication issued by or on behalf of the Commission to the reporting market shall constitute valid and effective service upon the foreign clearing member or foreign trader. The reporting market which has been served with, or to which there has been delivered, a communication issued by or on behalf of the Commission to a foreign clearing member or foreign trader shall transmit the communication promptly and in a manner which is reasonable under the circumstances, or in a manner specified by the Commission in the communication, to the foreign clearing member or foreign trader.

(1) It shall be unlawful for any such reporting market to permit a foreign clearing member or a foreign trader to clear or effect contracts, agreements or transactions on the facility or its clearing organization unless the reporting market prior thereto informs the foreign clearing member or foreign trader of the requirements of this section.

(2) The requirements of paragraphs (i) introductory text and (i)(1) of this section shall not apply to any contracts, transactions or agreements if the foreign clearing member or foreign trader has duly executed and maintains in effect a written agency agreement in compliance with this paragraph with a person domiciled in the United States and has provided a copy of the agreement to the reporting market prior to effecting or clearing any contract, agreement or transaction on the trading facility or its clearing organization. This agreement must authorize the person domiciled in the United States to serve as the agent

of the foreign clearing member or foreign trader for the purposes of accepting delivery and service of all communications issued by or on behalf of the Commission to the foreign clearing member or the foreign trader and must provide an address in the United States where the agent will accept delivery and service of communications from the Commission. This agreement must be filed with the Commission by the reporting market prior to permitting the foreign clearing member or the foreign trader to clear or effect any transactions in futures or option contracts. Unless otherwise specified by the Commission, the agreements required to be filed with the Commission shall be filed with the Secretary of the Commission at Three Lafayette Centre, 1155 21st Street, NW., Washington, DC 20581.

(3) A foreign clearing member or a foreign trader shall notify the Commission immediately if the written agency agreement is terminated, revoked, or is otherwise no longer in effect. If the reporting market knows or should know that the agreement has expired, been terminated, or is no longer in effect, the reporting market shall notify the Secretary of the Commission immediately. If the written agency agreement expires, terminates, or is not in effect, the reporting market, the foreign clearing member and the foreign trader shall be subject to the provisions of paragraphs (i) introductory text and (i)(1) of this section.

5. Add § 15.06 to read as follows:

**§ 15.06 Delegations.**

(a) The Commission hereby delegates, until the Commission orders otherwise, the authority to approve data processing media, as referenced in § 15.00(d), for data submissions to the Director of the Division of Market Oversight, to be exercised by such Director or by such other employee or employees of such Director as designated from time to time by the Director. The Director may submit to the Commission for its consideration any matter which has been delegated in this paragraph. Nothing in this paragraph prohibits the Commission, at its election, from exercising the authority delegated in this paragraph.

(b) [Reserved]

**PART 16—REPORTS BY REPORTING MARKETS**

6. The authority citation for part 16 is revised to read as follows:

**Authority:** 7 U.S.C. 2, 6a, 6c, 6g, 6i, 7, 7a and 12a, as amended by Title XIII of the Food, Conservation and Energy Act of 2008,

Pub. L. No. 110–246, 122 Stat. 1624 (June 18, 2008), unless otherwise noted.

7. In § 16.01, revise paragraphs (e)(1) and (e)(2) to read as follows:

**§ 16.01 Trading volume, open contracts, prices, and critical dates.**

\* \* \* \* \*

(e) *Publication of recorded information.* (1) Reporting markets shall make the information in paragraph (a) of this section readily available to the news media and the general public without charge, in a format that readily enables the consideration of such data, no later than the business day following the day to which the information pertains. The information in paragraphs (a)(4) through (a)(6) of this section shall be made readily available in a format that presents the information together.

(2) Reporting markets shall make the information in paragraphs (b)(1) and (b)(2) of this section readily available to the news media and the general public, and the information in paragraph (b)(3) of this section readily available to the general public, in a format that readily enables the consideration of such data, no later than the business day following the day to which the information pertains.

\* \* \* \* \*

8. Section 16.02 is added to read as follows:

**§ 16.02 Daily trade and supporting data reports.**

Reporting markets shall provide trade and supporting data reports to the Commission on a daily basis. Such reports shall include transaction-level trade data and related order information for each transaction that is executed on the reporting market. Reports shall also include time and sales data, reference files and other information as the Commission or its designee may require. All reports must be submitted at the time, and in the manner and format, and with the specific content specified by the Commission or its designee. Upon request, such information shall be accompanied by data that identifies or facilitates the identification of each trader for each transaction or order included in a submitted trade and supporting data report if the reporting market maintains such data.

9. In § 16.07, revise the heading and introductory text; and add paragraph (c) to read as follows:

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

The Commission hereby delegates, until the Commission orders otherwise, the authority set forth in paragraphs (a), (b) and (c) of this section to the Director

of the Division of Market Oversight, to be exercised by such Director or by such other employee or employees of such Director as may be designated from time to time by the Director. The Director of the Division of Market Oversight may submit to the Commission for its consideration any matter which has been delegated in this paragraph. Nothing in this paragraph prohibits the Commission, at its election, from exercising the authority delegated in this paragraph.

\* \* \* \* \*

(c) Pursuant to § 16.02, the authority to determine the specific content of any daily trade and supporting data report, request that such reports be accompanied by data that identifies or facilitates the identification of each trader for each transaction or order included in a submitted trade and supporting data report, and the time for the submission of and the manner and format of such reports.

**PART 17—REPORTS BY REPORTING MARKETS, FUTURES COMMISSION MERCHANTS, CLEARING MEMBERS, AND FOREIGN BROKERS**

10. The authority citation for part 17 is revised to read as follows:

**Authority:** 7 U.S.C. 2, 6a, 6c, 6d, 6f, 6g, 6i, 7, 7a and 12a, as amended by Title XIII of the Food, Conservation and Energy Act of 2008, Pub. L. No. 110–246, 122 Stat. 1624 (June 18, 2008), unless otherwise noted.

11. Revise the heading of part 17 as set forth above.

12. In § 17.00, revise paragraph (a) introductory text and paragraphs (a)(1), (b)(1), and (f); and add and reserve paragraph (c) to read as follows:

**§ 17.00 Information to be furnished by futures commission merchants, clearing members and foreign brokers.**

(a) *Special accounts—reportable futures and options positions, delivery notices, and exchanges of futures.* (1) Each futures commission merchant, clearing member and foreign broker shall submit a report to the Commission for each business day with respect to all special accounts carried by the futures commission merchant, clearing member or foreign broker, except for accounts carried on the books of another futures commission merchant or clearing member on a fully-disclosed basis. Except as otherwise authorized by the Commission or its designee, such report shall be made in accordance with the format and coding provisions set forth in paragraph (g) of this section. The report shall show each futures position traded in reliance on the exemption in section 2(h)(3) of the Act, separately for

each reporting market and for each future position traded in reliance on the exemption in section 2(h)(3) of the Act, and each put and call options position separately for each reporting market, expiration and strike price in each special account as of the close of market on the day covered by the report and, in addition, the quantity of exchanges of futures for commodities or for derivatives positions and the number of delivery notices issued for each such account by the clearing organization of a reporting market and the number stopped by the account. The report shall also show all positions in all contract months and option expirations of that same commodity on the same reporting market for which the special account is reportable.

\* \* \* \* \*

(b) \* \* \*

(1) *Accounts of eligible entities—*Accounts of eligible entities as defined in § 150.1 of this chapter that are traded by an independent account controller shall, together with other accounts traded by the independent account controller or in which the independent controller has a financial interest, be considered a single account.

\* \* \* \* \*

(c) [Reserved]

\* \* \* \* \*

(f) *Omnibus accounts.* If the total open long positions or the total open short positions for any future of a commodity carried in an omnibus account is a reportable position, the omnibus account is in Special Account status and shall be reported by the futures commission merchant or foreign broker carrying the account in accordance with paragraph (a) of this section.

\* \* \* \* \*

13. In § 17.03, revise the heading, the introductory text, and paragraphs (a) and (b) to read as follows:

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

The Commission hereby delegates, until the Commission orders otherwise, the authority set forth in the paragraphs below to the Director of the Division of Market Oversight to be exercised by such Director or by such other employee or employees of such Director as designated from time to time by the Director. The Director of the Division of Market Oversight may submit to the Commission for its consideration any matter which has been delegated in this paragraph. Nothing in this paragraph prohibits the Commission, at its election, from exercising the authority delegated in this paragraph.

(a) Pursuant to § 17.00(a) and (h), the authority to determine whether futures commission merchants, clearing members and foreign brokers can report the information required under paragraphs (a) and (h) of § 17.00 on series '01 forms or using some other format upon a determination that such person is unable to report the information using the format, coding structure or electronic data transmission procedures otherwise required.

(b) Pursuant to § 17.02, the authority to instruct or approve the time at which the information required under §§ 17.00 and 17.01 must be submitted by futures commission merchants, clearing members and foreign brokers provided that such persons are unable to meet the requirements set forth in §§ 17.01(g) and 17.02.

\* \* \* \* \*

14. In § 17.04, revise the heading, paragraph (a), and paragraph (b)(1)(ii) to read as follows:

**§ 17.04 Reporting omnibus accounts to reporting firms.**

(a) Any futures commission merchant, clearing member or foreign broker who establishes an omnibus account with another futures commission merchant, clearing member or foreign broker shall report to that futures commission merchant, clearing member or foreign broker the total open long positions and the total open short positions in each future of a commodity and, for commodity options transactions, the total open long put options, the total open short put options, the total open long call options, and the total open short call options for each commodity options expiration date and each strike price in such account at the close of trading each day. The information required by this section shall be reported in sufficient time to enable the futures commission merchant, clearing member or foreign broker with whom the omnibus account is established to comply with the regulations of this part and the reporting requirements established by the reporting markets.

(b) \* \* \*

(1) \* \* \*

(ii) The account is an omnibus account of another futures commission merchant, clearing member or foreign broker; or

\* \* \* \* \*

**PART 18—REPORTS BY TRADERS**

15. The authority citation for part 18 continues to read as follows:

**Authority:** 7 U.S.C. 2, 4, 5, 6a, 6c, 6f, 6g, 6i, 6k, 6m, 6n, 12a and 19, as amended by Title XIII of the Food, Conservation and

Energy Act of 2008, Pub. L. No. 110–246, 122 Stat. 1624 (June 18, 2008); 5 U.S.C. 552 and 552(b), unless otherwise noted.

16. Revise § 18.01 to read as follows:

**§ 18.01 Interest in or control of several accounts.**

If any trader holds, has a financial interest in or controls positions in more than one account, whether carried with the same or with different futures commission merchants or foreign brokers, all such positions and accounts shall be considered as a single account for the purpose of determining whether such trader has a reportable position and, unless instructed otherwise in the special call to report under § 18.00 for the purpose of reporting.

17. In § 18.04, revise paragraphs (a)(7) and (b)(3)(i) to read as follows:

**§ 18.04 Statement of reporting trader.**

\* \* \* \* \*

(a) \* \* \*

(7) The names and locations of all futures commission merchants, clearing members, introducing brokers, and foreign brokers through whom accounts owned or controlled by the reporting trader are carried or introduced at the time of filing a Form 40, if such accounts are carried through more than one futures commission merchant, clearing member or foreign broker or carried through more than one office of the same futures commission merchant, clearing member or foreign broker, or introduced by more than one introducing broker clearing accounts through the same futures commission merchant, and the name of the reporting trader's account executive at each firm or office of the firm.

(b) \* \* \*

(3) \* \* \*

(i) Commercial activity associated with use of the option or futures market (such as and including production, merchandising or processing of a cash commodity, asset or liability risk management by depository institutions, or security portfolio risk management).

\* \* \* \* \*

18. In § 18.05, revise paragraphs (a)(2), (a)(3), and (a)(4) to read as follows:

**§ 18.05 Maintenance of books and records.**

(a) \* \* \*

(2) Over the counter or pursuant to sections 2(d), 2(g) or 2(h)(1)–(2) of the Act or part 35 of this chapter;

(3) On exempt commercial markets operating pursuant to sections 2(h)(3)–(5) of the Act;

(4) On exempt boards of trade operating pursuant to section 5d of the Act; and

\* \* \* \* \*

**PART 19—REPORTS BY PERSONS HOLDING BONA FIDE HEDGE POSITIONS PURSUANT TO § 1.3(z) OF THIS CHAPTER AND BY MERCHANTS AND DEALERS IN COTTON**

19. The authority citation for part 19 continues to read as follows:

**Authority:** 7 U.S.C. 6g(a), 6i, and 12a(5), as amended by Title XIII of the Food, Conservation and Energy Act of 2008, Pub. L. No. 110–246, 122 Stat. 1624 (June 18, 2008), unless otherwise noted.

20. In § 19.00, revise paragraph (a) to read as follows:

**§ 19.00 General provisions.**

(a) Who must file series '04 reports. The following persons are required to file series '04 reports:

(1) All persons holding or controlling futures and option positions that are reportable pursuant to § 15.00(n)(2) of this chapter and any part of which constitute bona fide hedging positions as defined in § 1.3(z) of this chapter;

(2) Merchants and dealers of cotton holding or controlling positions for futures delivery in cotton that are reportable pursuant to § 15.00(n)(1)(i) of this chapter, or

(3) All persons holding or controlling positions for future delivery that are reportable pursuant to § 15.00(n)(1) of this chapter who have received a special call for series '04 reports from the Commission or its designee. Filings in response to a special call shall be made within one business day of receipt of the special call unless otherwise specified in the call. For the purposes of this paragraph, the Commission hereby delegates to the Director of the Division of Market Oversight, or to such other person designated by the Director, authority to issue calls for series '04 reports.

\* \* \* \* \*

21. In § 19.01, revise paragraph (b) introductory text and paragraph (b)(1) to read as follows:

**§ 19.01 Reports on stocks and fixed price purchases and sales pertaining to futures positions in wheat, corn, oats, soybeans, soybean oil, soybean meal or cotton.**

\* \* \* \* \*

(b) *Time and place of filing reports*—Except for reports filed in response to special calls made under § 19.00(a)(3), each report shall be made monthly, as of the close of business on the last Friday of the month, and filed at the appropriate Commission office specified in paragraph (b)(1) or (2) of this section not later than the second business day following the date of the report in the case of the 304 report and not later than the third business day following the

date of the report in the case of the 204 report. Reports may be transmitted by facsimile or, alternatively, information on the form may be reported to the appropriate Commission office by telephone and the report mailed to the same office, not later than midnight of its due date.

(1) CFTC Form 204 reports with respect to transactions in wheat, corn, oats, soybeans, soybean meal and soybean oil should be sent to the Commission's office in Chicago, IL, unless otherwise specifically authorized by the Commission or its designee.

\* \* \* \* \*

**PART 21—SPECIAL CALLS**

22. The authority citation for part 21 continues to read as follows:

**Authority:** 7 U.S.C. 1a, 2, 2a, 4, 6a, 6c, 6f, 6g, 6i, 6k, 6m, 6n, 7, 7a, 12a, 19 and 21, as amended by Title XIII of the Food, Conservation and Energy Act of 2008, Pub. L. No. 110–246, 122 Stat. 1624 (June 18, 2008); 5 U.S.C. 552 and 552(b), unless otherwise noted.

23. Revise § 21.01 to read as follows:

**§ 21.01 Special calls for information on controlled accounts from futures commission merchants, clearing members and introducing brokers.**

Upon call by the Commission, each futures commission merchant, clearing member and introducing broker shall file with the Commission the names and addresses of all persons who, by power of attorney or otherwise, exercise trading control over any customer's account in commodity futures or commodity options on any reporting market.

24. In § 21.02, revise the heading, introductory text, and paragraphs (f) and (i) to read as follows:

**§ 21.02 Special calls for information on open contracts in accounts carried or introduced by futures commission merchants, clearing members, members of reporting markets, introducing brokers, and foreign brokers.**

Upon special call by the Commission for information relating to futures or option positions held or introduced on the dates specified in the call, each futures commission merchant, clearing member, member of a reporting market, introducing broker, or foreign broker, and, in addition, for option information, each reporting market, shall furnish to the Commission the following information concerning accounts of traders owning or controlling such futures or option positions, except for accounts carried on a fully disclosed basis by another futures commission

merchant or clearing member, as may be specified in the call:

\* \* \* \* \*

(f) The number of open futures or option positions introduced or carried in each account, as specified in the call;

\* \* \* \* \*

(i) As applicable, the following identifying information:

(1) Whether a trader who holds commodity futures or option positions is classified as a commercial or as a noncommercial trader for each commodity futures or option contract;

(2) Whether the open commodity futures or option contracts are classified as speculative, spreading (straddling), or hedging; and

(3) Whether any of the accounts in question are omnibus accounts and, if so, whether the originator of the omnibus account is another futures commission merchant, clearing member or foreign broker.

\* \* \* \* \*

25. Amend § 21.03 as follows:

A. Revise the heading and paragraphs (a), (b), (c) and (d);

B. Revise paragraph (e) introductory text and paragraphs (e)(1) introductory text, (e)(1)(iv) and (e)(1)(v); and

C. Revise paragraphs (f), (g) and (h) to read as follows:

**§ 21.03 Selected special calls—duties of foreign brokers, domestic and foreign traders, futures commission merchants, clearing members, introducing brokers, and reporting markets.**

(a) For purposes of this section, the term “accounts of a futures commission merchant, clearing member or foreign broker” means all open contracts and transactions in futures and options on the records of the futures commission merchant, clearing member or foreign broker; the term “beneficial interest” means having or sharing in any rights, obligations or financial interest in any futures or options account; the term “customer” means any futures commission merchant, clearing member, introducing broker, foreign broker, or trader for whom a futures commission merchant, clearing member or reporting market that is a registered entity under section 1a(29)(E) of the Act makes or causes to be made a futures or options contract. Paragraphs (e), (g) and (h) of this section shall not apply to any futures commission merchant, clearing member or customer whose books and records are open at all times to inspection in the United States by any representative of the Commission.

(b) It shall be unlawful for a futures commission merchant to open a futures or options account or to effect transactions in futures or options

contracts for an existing account, or for an introducing broker to introduce such an account, for any customer for whom the futures commission merchant or introducing broker is required to provide the explanation provided for in § 15.05(c) of this chapter, or for a reporting market that is a registered entity under section 1a(29)(E) of the Act, to cause to open an account in a contract traded in reliance on the exemption in section 2(h)(3) of the Act or to cause to be effected transactions in a contract traded in reliance on the exemption in section 2(h)(3) of the Act for an existing account for any person that is a foreign clearing member or foreign trader, until the futures commission merchant, introducing broker, clearing member, or reporting market has explained fully to the customer, in any manner that such persons deem appropriate, the provisions of this section.

(c) Upon a determination by the Commission that information concerning accounts may be relevant information in enabling the Commission to determine whether the threat of a market manipulation, corner, squeeze, or other market disorder exists on any reporting market, the Commission may issue a call for information from a futures commission merchant, clearing member, introducing broker or customer pursuant to the provisions of this section.

(d) In the event the call is issued to a foreign broker, foreign clearing member or foreign trader, its agent, designated pursuant to § 15.05 of this chapter, shall, if directed, promptly transmit calls made by the Commission pursuant to this section by electronic mail or a similarly expeditious means of communication.

(e) The futures commission merchant, clearing member, introducing broker, or customer to whom the special call is issued must provide to the Commission the information specified below for the commodity, reporting market and delivery months or option expiration dates named in the call. Such information shall be filed at the place and within the time specified by the Commission.

(1) For each account of a futures commission merchant, clearing member, introducing broker, or foreign broker, including those accounts in the name of the futures commission merchant, clearing member or foreign broker, on the dates specified in the call issued pursuant to this section, such persons shall provide the Commission with the following information:

\* \* \* \* \*



(iv) Whether the account is carried for and in the name of another futures commission merchant, clearing member, introducing broker, or foreign broker; and

(v) For the accounts which are not carried for and in the name of another futures commission merchant, clearing member, introducing broker, or foreign broker, the name and address of any other person who controls the trading of the account, and the name and address of any person who has a ten percent or more beneficial interest in the account.

\* \* \* \* \*

(f) If the Commission has reason to believe that any person has not responded as required to a call made pursuant to this section, the Commission in writing may inform the reporting market specified in the call and that reporting market shall prohibit the execution of, and no futures commission merchant, clearing member, introducing broker, or foreign broker shall effect a transaction in connection with trades on the reporting market and in the months or expiration dates specified in the call for or on behalf of the futures commission merchant or customer named in the call, unless such trades offset existing open contracts of such futures commission merchant or customer.

(g) Any person named in a special call that believes he or she is or may be adversely affected or aggrieved by action taken by the Commission under paragraph (f) of this section shall have the opportunity for a prompt hearing after the Commission acts. That person may immediately present in writing to the Commission for its consideration any comments or arguments concerning the Commission's action and may present for Commission consideration any documentary or other evidence that person deems appropriate. Upon request, the Commission may, in its discretion, determine that an oral hearing be conducted to permit the further presentation of information and views concerning any matters by any or all such persons. The oral hearing may be held before the Commission or any person designated by the Commission, which person shall cause all evidence to be reduced to writing and forthwith transmit the same and a recommended decision to the Commission. The Commission's directive under paragraph (f) of this section shall remain in effect unless and until modified or withdrawn by the Commission.

(h) If, during the course of or after the Commission acts pursuant to paragraph (f) of this section, the Commission determines that it is appropriate to

undertake a proceeding pursuant to section 6(c) of the Act, the Commission shall issue a complaint in accordance with the requirements of section 6(c), and, upon further determination by the Commission that the conditions described in paragraph (c) of this section still exist, a hearing pursuant to section 6(c) of the Act shall commence no later than five business days after service of the complaint. In the event the person served with the complaint under section 6(c) of the Act has, prior to the commencement of the hearing under section 6(c) of the Act, sought a hearing pursuant to paragraph (g) of this section and the Commission has determined to accord him such a hearing, the two hearings shall be conducted simultaneously. Nothing in this section shall preclude the Commission from taking other appropriate action under the Act or the Commission's regulations thereunder, including action under section 6(c) of the Act, regardless of whether the conditions described in paragraph (c) of this section still exist, and no ruling issued in the course of a hearing pursuant to paragraph (g) or this section shall constitute an estoppel against the Commission in any other action.

26. Revise § 21.04 to read as follows:

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

The Commission hereby delegates, until the Commission orders otherwise, the special call authority set forth in §§ 21.01 and 21.02 the Director of the Division of Market Oversight to be exercised by such Director or by such other employee or employees of such Director as designated from time to time by the Director. The Director of the Division of Market Oversight may submit to the Commission for its consideration any matter which has been delegated in this paragraph. Nothing in this section shall be deemed to prohibit the Commission, at its election, from exercising the authority delegated in this section to the Director.

**PART 36—EXEMPT MARKETS**

27. The authority citation for part 36 is revised to read as follows:

**Authority:** 7 U.S.C. 2, 2(h)(7), 6, 6c and 12a, as amended by Title XIII of the Food, Conservation and Energy Act of 2008, Pub. L. No. 110-246, 122 Stat. 1624 (June 18, 2008).

28–30. Section 36.3 is amended by revising paragraphs (b) and (c), and adding paragraph (d), to read as follows:

**§ 36.3 Exempt commercial markets.**

\* \* \* \* \*

(b) *Required information.*

(1) *All electronic trading facilities.* A facility operating in reliance on the exemption in section 2(h)(3) of the Act, initially and on an on-going basis, must:

(i) Provide the Commission with the terms and conditions, as defined in part 40.1(i) of this chapter and product descriptions for each agreement, contract or transaction listed by the facility in reliance on the exemption set forth in section 2(h)(3) of the Act, as well as trading conventions, mechanisms and practices;

(ii) Provide the Commission with information explaining how the facility meets the definition of "trading facility" contained in section 1a(33) of the Act and provide the Commission with access to the electronic trading facility's trading protocols, in a format specified by the Commission;

(iii) Demonstrate to the Commission that the facility requires, and will require, with respect to all current and future agreements, contracts and transactions, that each participant agrees to comply with all applicable laws; that the authorized participants are "eligible commercial entities" as defined in section 1a(11) of the Act; that all agreements, contracts and transactions are and will be entered into solely on a principal-to-principal basis; and that the facility has in place a program to routinely monitor participants' compliance with these requirements;

(iv) At the request of the Commission, provide any other information that the Commission, in its discretion, deems relevant to its determination whether an agreement, contract, or transaction performs a significant price discovery function; and

(v) File with the Commission annually, no later than the end of each calendar year, a completed copy of CFTC Form 205—Exempt Commercial Market Annual Certification. The information submitted in Form 205 shall include:

(A) A statement indicating whether the electronic trading facility continues to operate under the exemption; and

(B) A certification that affirms the accuracy of and/or updates the information contained in the previous Notification of Operation as an Exempt Commercial Market.

(2) *Electronic trading facilities trading or executing agreements, contracts or transactions other than significant price discovery contracts.* In addition to the requirements of paragraph (b)(1) of this section, a facility operating in reliance on the exemption in section 2(h)(3) of the Act, with respect to agreements, contracts or transactions that have not been determined to perform significant

price discovery function, initially and on an on-going basis, must:

(i) Identify to the Commission those agreements, contracts and transactions conducted on the electronic trading facility with respect to which it intends, in good faith, to rely on the exemption in section 2(h)(3) of the Act, and which averaged five trades per day or more over the most recent calendar quarter; and, with respect to such agreements, contracts and transactions, either:

(A) Submit to the Commission, in a form and manner acceptable to the Commission, a report for each business day, showing for each such agreement, contract or transaction executed the following information:

(1) The underlying commodity, the delivery or price-basing location specified in the agreement, contract or transaction maturity date, whether it is a financially settled or physically delivered instrument, and the date of execution, time of execution, price, and quantity;

(2) Total daily volume and, if cleared, open interest;

(3) For an option instrument, in addition to the foregoing information, the type of option (*i.e.*, call or put) and strike prices; and

(4) Such other information as the Commission may determine.

Each such report shall be electronically transmitted weekly, within such time period as is acceptable to the Commission after the end of the week to which the data applies; or

(B) (1) Provide to the Commission, in a form and manner acceptable to the Commission, electronic access to those transactions conducted on the electronic trading facility in reliance on the exemption in section 2(h)(3) of the Act, and meeting the average five trades per day or more threshold test of this section, which would allow the Commission to compile the information described in paragraph (b)(2)(i)(A) of this section and create a permanent record thereof;

(2) Maintain a record of allegations or complaints received by the electronic trading facility concerning instances of suspected fraud or manipulation in trading activity conducted in reliance on the exemption set forth in section 2(h)(3) of the Act. The record shall contain the name of the complainant, if provided, date of the complaint, market instrument, substance of the allegations, and name of the person at the electronic trading facility who received the complaint;

(3) Provide to the Commission, in the form and manner prescribed by the Commission, a copy of the record of each complaint received pursuant to

paragraph (b)(2)(ii) of this section that alleges, or relates to, facts that would constitute a violation of the Act or Commission regulations. Such copy shall be provided to the Commission no later than 30 calendar days after the complaint is received. Provided, however, that in the case of a complaint alleging, or relating to, facts that would constitute an ongoing fraud or market manipulation under the Act or Commission regulations, such copy shall be provided to the Commission within three business days after the complaint is received; and

(4) Provide to the Commission on a quarterly basis, within 15 calendar days of the close of each quarter, a list of each agreement, contract or transaction executed on the electronic trading facility in reliance on the exemption set forth in section 2(h)(3) of the Act and indicate for each such agreement, contract or transaction the contract terms and conditions, the contract's average daily trading volume, and the most recent open interest figures.

(3) *Electronic trading facilities trading or executing significant price discovery contracts.* In addition to the requirements of paragraph (b)(1) of this section, if the Commission determines that a facility operating in reliance on the exemption in section 2(h)(3) of the Act trades or executes an agreement, contract or transaction that performs a significant price discovery function, the facility must, with respect to any significant price discovery contract, publish and provide to the Commission the information required by § 16.01 of this chapter.

(4) *Delegation of authority.* The Commission hereby delegates, until the Commission orders otherwise, the authority to determine the form and manner of submitting the required information under paragraphs (b)(1) through (3) of this section, to the Director of the Division of Market Oversight and such members of the Commission's staff as the Director may designate. The Director may submit to the Commission for its consideration any matter that has been delegated by this paragraph. Nothing in this paragraph prohibits the Commission, at its election, from exercising the authority delegated in this paragraph.

(5) *Special calls.*

(i) All information required upon special call of the Commission under section 2(h)(5)(B)(iii) of the Act shall be transmitted at the time and to the office of the Commission as may be specified in the call.

(ii) The Commission hereby delegates, until the Commission orders otherwise, the authority to make special calls as set

forth in section 2(h)(5)(B)(iii) of the Act to the Directors of the Division of Market Oversight, the Division of Clearing and Intermediary Oversight, and the Division of Enforcement to be exercised by each such Director or by such other employee or employees as the Director may designate. The Directors may submit to the Commission for its consideration any matter that has been delegated in this paragraph. Nothing in this paragraph prohibits the Commission, at its election, from exercising the authority delegated in this paragraph.

(6) *Subpoenas to foreign persons.* A foreign person whose access to an electronic trading facility is limited or denied at the direction of the Commission based on the Commission's belief that the foreign person has failed timely to comply with a subpoena as provided under section 2(h)(5)(C)(ii) of the Act shall have an opportunity for a prompt hearing under the procedures provided in § 21.03(b) and (h) of this chapter.

(7) *Prohibited representation.* An electronic trading facility relying upon the exemption in section 2(h)(3) of the Act, with respect to agreements, contracts or transactions that are not significant price discovery contracts, shall not represent to any person that it is registered with, designated, recognized, licensed or approved by the Commission.

(c) *Significant price discovery contracts.*

(1) *Criteria for significant price discovery determination.* The Commission may determine, in its discretion, that an electronic trading facility operating a market in reliance on the exemption in section 2(h)(3) of the Act performs a significant price discovery function for transactions in the cash market for a commodity underlying any agreement, contract or transaction executed or traded on the facility. In making such a determination, the Commission shall consider, as appropriate:

(i) *Price linkage.* The extent to which the agreement, contract or transaction uses or otherwise relies on a daily or final settlement price, or other major price parameter, of a contract or contracts listed for trading on or subject to the rules of a designated contract market or a derivatives transaction execution facility to value a position, transfer or convert a position, cash or financially settle a position, or close out a position;

(ii) *Arbitrage.* The extent to which the price for the agreement, contract or transaction is sufficiently related to the price of a contract or contracts listed for

trading on or subject to the rules of a designated contract market or derivatives transaction execution facility, or a significant price discovery contract or contracts trading on or subject to the rules of an electronic trading facility, so as to permit market participants to effectively arbitrage between the markets by simultaneously maintaining positions or executing trades in the contracts on a frequent and recurring basis;

(iii) *Material price reference.* The extent to which, on a frequent and recurring basis, bids, offers, or transactions in a commodity are directly based on, or are determined by referencing, the prices generated by agreements, contracts or transactions being traded or executed on the electronic trading facility;

(iv) *Material liquidity.* The extent to which the volume of agreements, contracts or transactions in the commodity being traded on the electronic trading facility is sufficient to have a material effect on other agreements, contracts or transactions listed for trading on or subject to the rules of a designated contract market, a derivatives transaction execution facility, or an electronic trading facility operating in reliance on the exemption in section 2(h)(3) of the Act;

(v) *Other material factors* [Reserved].

(2) *Notification of possible significant price discovery contract conditions.* An electronic trading facility operating in reliance on section 2(h)(3) of the Act shall promptly notify the Commission, and such notification shall be accompanied by supporting information or data concerning any contract that:

(i) Averaged five trades per day or more over the most recent calendar quarter; and

(ii) (A) For which the exchange sells its price information regarding the contract to market participants or industry publications; or

(B) Whose daily closing or settlement prices on 95 percent or more of the days in the most recent quarter were within 2.5 percent of the contemporaneously determined closing, settlement or other daily price of another agreement, contract or transaction.

(3) *Procedure for significant price discovery determination.* Before making a final price discovery determination under this paragraph, the Commission shall publish notice in the **Federal Register** that it intends to undertake a determination with respect to whether a particular agreement, contract or transaction performs a significant price discovery function and to receive written data, views and arguments relevant to its determination from the

electronic trading facility and other interested persons. Any such written data, views and arguments shall be filed with the Secretary of the Commission, in the form and manner specified by the Commission, within 30 calendar days of publication of notice in the **Federal Register** or within such other time specified by the Commission. After consideration of all relevant information, the Commission shall issue an order explaining its determination whether the agreement, contract or transaction executed or traded by the electronic trading facility performs a significant price discovery function under the criteria specified in paragraphs (c)(1)(i) through (v) of this section.

(4) *Compliance with Core Principles.* Following the issuance of an order by the Commission that the electronic trading facility executes or trades an agreement, contract or transaction that performs a significant price discovery function, the electronic trading facility must demonstrate, with respect to that agreement, contract or transaction, compliance with the Core Principles under section 2(h)(7)(C) of the Act and the applicable provisions of this part. If the Commission's order represents the first time it has determined that the electronic trading facility's agreement, contract or transaction performs a significant price discovery function, the facility must submit a written demonstration of compliance with the Core Principles within 90 calendar days of the date of the Commission's order. For subsequent determinations by the Commission that the electronic trading facility has an additional agreement, contract or transaction that performs a significant price discovery function, the facility must submit a written demonstration of compliance with the Core Principles within 15 calendar days of the date of the Commission's order. Attention is directed to Appendix B of this part for guidance on and acceptable practices for complying with the Core Principles. Submissions demonstrating how the electronic trading facility complies with the Core Principles with respect to its significant price discovery contract must be filed with the Secretary of the Commission at its Washington, DC headquarters. Submissions must include the following:

(i) A written certification that the significant price discovery contract(s) complies with the Act and regulations thereunder;

(ii) A copy of the electronic trading facility's rules (as defined in § 40.1 of this chapter) and any technical manuals, other guides or instructions for users of, or participants in, the market, including

minimum financial standards for members or market participants. Subsequent rule changes must be certified by the electronic trading facility pursuant to section 5c(c) of the Act and § 40.6 of this chapter. The electronic trading facility also may request Commission approval of any rule changes pursuant to section 5c(c) of the Act and § 40.5 of this chapter;

(iii) A description of the trading system, algorithm, security and access limitation procedures with a timeline for an order from input through settlement, and a copy of any system test procedures, tests conducted, test results and contingency or disaster recovery plans;

(iv) A copy of any documents pertaining to or describing the electronic trading system's legal status and governance structure, including governance fitness information;

(v) An executed or executable copy of any agreements or contracts entered into or to be entered into by the electronic trading facility, including partnership or limited liability company, third-party regulatory service, or member or user agreements, that enable or empower the electronic trading facility to comply with a Core Principle;

(vi) A copy of any manual or other document describing, with specificity, the manner in which the trading facility will conduct trade practice, market and financial surveillance;

(vii) To the extent that any of the items in paragraphs (c)(4)(ii) through (vi) of this section raise issues that are novel, or for which compliance with a core principle is not self-evident, an explanation of how that item satisfies the applicable core principle or principles. The electronic trading facility must identify with particularity information in the submission that will be subject to a request for confidential treatment pursuant to § 145.09 of this chapter. The electronic trading facility must follow the procedures specified in § 40.8 of this chapter with respect to any information in its submission for which confidential treatment is requested.

(5) *Determination of compliance with core principles.* The Commission shall take into consideration differences between cleared and uncleared significant price discovery contracts when reviewing the implementation of the Core Principles by an electronic trading facility. The electronic facility also has reasonable discretion in accounting for differences between cleared and uncleared significant price discovery contracts when establishing the manner in which it complies with the Core Principles.

(6) *Information relating to compliance with core principles.* Upon request by the Commission, an electronic trading facility trading a significant price discovery contract shall file with the Commission a written demonstration, containing such supporting data, information and documents, in the form and manner and within such time as the Commission may specify, that the electronic trading facility is in compliance with one or more core principles as specified in the request, or that is otherwise requested by the Commission to enable the Commission to satisfy its obligations under the Act.

(7) *Enforceability.* An agreement, contract or transaction entered into on or pursuant to the rules of an electronic trading facility trading or executing a significant price discovery contract shall not be void, voidable, subject to rescission or otherwise invalidated or rendered unenforceable as a result of:

(i) A violation by the electronic trading facility of the provisions of section 2(h) of the Act or this part; or

(ii) Any Commission proceeding to alter or supplement a rule, term or condition under section 8a(7) of the Act, to declare an emergency under section 8a(9) of the Act, or any other proceeding the effect of which is to alter, supplement or require an electronic trading facility to adopt a specific term or condition, trading rule or procedure, or to take or refrain from taking a specific action.

(8) *Procedures for vacating a determination of a significant price discovery function.*

(i) *By the electronic trading facility.* An electronic trading facility that executes or trades an agreement, contract or transaction that the Commission has determined performs a significant price discovery function under paragraph (c)(3) of this section may petition the Commission to vacate that determination. The petition shall demonstrate that the agreement, contract or transaction no longer performs a significant price discovery function under the criteria specified in paragraph (c)(1) of this section, and has not done so for at least the prior 12 months. An electronic trading facility shall not petition for a vacation of a significant price discovery determination more frequently than once every 12 months.

(ii) *By the Commission.* The Commission may, on its own initiative, begin vacation proceedings if it believes that an agreement, contract or transaction has not performed a significant price discovery function for at least the prior 12 months.

(iii) *Procedure.* Before making a final determination whether an agreement, contract or transaction has ceased to perform a significant price discovery function, the Commission shall publish notice in the **Federal Register** that it intends to undertake such a determination and to receive written data, views and arguments relevant to its determination from the electronic trading facility and other interested persons. Written submissions shall be filed with the Secretary of the Commission in the form and manner specified by the Commission, within 30 calendar days of publication of notice in the **Federal Register** or within such other time specified by the Commission. After consideration of all relevant information, the Commission shall issue an order explaining its determination whether the agreement, contract or transaction has ceased to perform a significant price discovery function and, if so, vacating its prior order. If such an order issues, and the Commission subsequently determines, on its own initiative or after notification by the electronic trading facility, that the agreement, contract or transaction that was subject to the vacation order again performs a significant price discovery function, the electronic trading facility must comply with the Core Principles within 15 calendar days of the date of the Commission's order.

(iv) *Automatic vacation of significant price discovery determination.*

Regardless of whether a proceeding to vacate has been initiated, any significant price discovery contract that has no open interest and in which no trading has occurred for a period of 12 complete and consecutive calendar months shall, without further proceedings, no longer be considered to be a significant price discovery contract.

(d) *Commission review.* The Commission shall, at least annually, evaluate as appropriate agreements, contracts or transactions conducted on an electronic trading facility in reliance on the exemption provided in section 2(h)(3) of the Act to determine whether they serve a significant price discovery function as described in paragraph (c)(1) of this section 31. Part 36 is amended by adding a new Appendix A to read as follows:

#### **Appendix A to Part 36—Guidance on Significant Price Discovery Contracts**

1. Section 2(h)(7) of the CEA specifies four factors that the Commission must consider, as appropriate, in making a determination that a contract is performing a significant price discovery function. The four factors prescribed by the statute are: Price Linkage;

Arbitrage; Material Price Reference; and Material Liquidity.

2. Not all listed factors must be present to support a determination that a contract performs a significant price discovery function. Moreover, the statutory language neither prioritizes the factors nor specifies the degree to which a significant price discovery contract must conform to the various factors. Congress has indicated that it intends that the Commission should not make a determination that an agreement, contract or transaction performs a significant price discovery function on the basis of the Price Linkage factor unless the agreement, contract or transaction also has sufficient volume to impact other regulated contracts or to become an independent price reference or benchmark that is regularly utilized by the public. The Commission believes that the Arbitrage and Material Price Reference factors can be considered separately from each other. That is, the Commission could make a determination that a contract serves a significant price discovery function based on the presence of one of these factors and the absence of the other. The presence of any of these factors, however, would not necessarily be sufficient to establish the contract as a significant price discovery contract. The fourth factor, Liquidity, would be considered in conjunction with the arbitrage and linkage factors as a significant amount of liquidity presumably would be necessary for a contract to perform a significant price discovery function in conjunction with these factors.

3. These factors do not lend themselves to a mechanical checklist or formulaic analysis. Accordingly, this guidance is intended to illustrate which factors, or combinations of factors, the Commission will look to when determining that a contract is performing a significant price discovery function, and under what circumstances the presence of a particular factor or factors would be sufficient to support such a determination.

(A) *MATERIAL LIQUIDITY—The extent to which the volume of agreements, contracts or transactions in the commodity being traded on the electronic trading facility is sufficient to have a material effect on other agreements, contracts or transactions listed for trading on or subject to the rules of a designated contract market, a derivatives transaction execution facility, or an electronic trading facility operating in reliance on the exemption in section 2(h)(3) of the Act.*

(1) Liquidity is a broad concept that captures the ability to transact immediately with little or no price concession. Traditionally, objective measures of trading such as volume or open interest have been used as measures of liquidity. So, for example, a market in which trades occur multiple times per minute at prices that differ by only fractions of a cent normally would be considered highly liquid, since presumably a trader could quickly execute a trade at a price that was approximately the same as the price for other recently executed trades. Other factors also will affect the characterization of liquidity, such as whether a large trade—e.g., 100 contracts versus 1 contract—could be executed without a significant price concession. For example,

having to wait a day to sell 1000 bushels of corn may be considered an illiquid market while waiting a day to sell a home may be considered quite liquid. Thus, quantifying the levels of immediacy and price concession that would define material liquidity may differ from one market or commodity to another.

(2) The Commission believes that material liquidity alternatively can be identified by the impact liquidity exhibits through observed prices. In markets where material liquidity exists, a more or less continuous stream of prices can be observed and the prices should be similar. For example, if the trading of a contract occurs on average five times a day, there will be on average five observed prices for the contract per day. If the market is liquid in terms of traders having to make little in the way of price concessions to execute these trades, the prices of this contract should be similar to those observed for similar or related contracts traded in liquid markets elsewhere. Thus, in making determinations that contracts have material liquidity, the Commission will look to transaction prices, both in terms of how often prices are observed and the extent to which observed prices tend to correlate with other contemporaneous prices.

(3) The Commission anticipates that material liquidity will frequently be a consideration in evaluating whether a contract is a significant price discovery contract; however, there may be circumstances in which other factors so dominate the conclusion that a contract is serving a significant price discovery function that a finding of material liquidity in the contract would not be necessary. Circumstances in which this might arise are discussed with respect to the assessment of other factors below.

(4) Finally, material liquidity itself would not be sufficient to make a determination that a contract is a significant price discovery contract, but combined with other factors it can serve as a guidepost indicating which contracts are functioning as significant price discovery contracts. As further discussed below, material liquidity, as reflected through the prices of linked or arbitrated contracts, will be a primary consideration in determining whether such contracts are significant price discovery contracts.

*(B) PRICE LINKAGE—The extent to which the agreement, contract or transaction uses or otherwise relies on a daily or final settlement price, or other major price parameter, of a contract or contracts listed for trading on or subject to the rules of a designated contract market or a derivatives transaction execution facility to value a position, transfer or convert a position, cash or financially settle a position, or close out a position.*

(1) A price-linked contract is a contract that relies on a contract traded on another trading facility to settle, value or otherwise offset the price-linked contract. The link may involve a one-to-one linkage, in that the value of the linked contract is based on a single contract's price, or it may involve multiple contracts. An example of a multiple contract linkage might be where the settlement price is calculated as an index of

prices obtained from a basket of contracts traded on other exchanges.

(2) For a linked contract, the mere fact that a contract is linked to another contract will not be sufficient to support a determination that a contract performs a significant price discovery function. To assess whether such a determination is warranted, the Commission will examine the relationship between transaction prices of the linked contract and the prices of the referenced contract(s). The Commission believes that where material liquidity exists, prices for the linked contract would be observed to be substantially the same as or move substantially in conjunction with the prices of the referenced contract(s). Where such price characteristics are observed on an ongoing basis, the Commission would expect to determine that the linked contract is a significant price discovery contract.

(3) As an example, where the Commission has observed price linkage, it will next consider whether transactions were occurring on a daily basis for the linked contract in material volumes. (Conversely, where volume has increased noticeably in a particular contract, the Commission would look for linkage) The ultimate level of volume that would be considered material for purposes of deeming a contract a significant price discovery contract will likely differ from one contract to another depending on the characteristics of the underlying commodity and the overall size of the physical market in which it is traded. At a minimum, however, the Commission will consider a linked contract which has volume equal to 5% of the volume of trading in the contract to which it is linked to have sufficient volume potentially to be deemed a significant price discovery contract. In combination with this volume level, the Commission will also examine the relationship between prices of the linked contract and the contract to which it is linked to determine whether a contract is serving a significant price discovery function. As a threshold, the Commission will consider a 2.5 percent price range for 95 percent of contemporaneously determined closing, settlement, or other daily prices over the most recent quarter to be sufficiently close for a linked contract potentially to be deemed a significant price discovery contract. For example, if, over the most recent quarter, it was found that 95 percent of the closing, settlement, or other daily prices of the contract, which have been calculated using transaction prices, were within 2.5 percent of the contemporaneously determined closing, settlement, or other daily prices of a contract to which it was linked, the Commission potentially would consider the contract to perform a significant price discovery function.

(4) If, in the example above, the Commission determines that material volume existed, it will examine the relationship between the prices of the linked contracts and the referenced contracts. If it finds that the transaction prices of the linked contract were consistently within a small percentage of the referenced contract or index of contracts that was being referenced, the Commission will be likely to find the linked

contract to be a significant price discovery contract. As a threshold, the Commission will consider a 2.5 percent price range for 95 percent of closing or settlement prices over the most recent quarter to be sufficiently close for a linked contract to potentially be deemed a significant price discovery contract. For example, if, over the most recent quarter, it was found that on 95 percent or more of the days the closing or settlement price of the contract, which has been calculated using transaction prices, was within 2.5 percent of the closing or settlement price of a contract to which it was linked, the Commission potentially will consider the contract to perform a significant price discovery function.

*(C) ARBITRAGE CONTRACTS—The extent to which the price for the agreement, contract or transaction is sufficiently related to the price of a contract or contracts listed for trading on or subject to the rules of a designated contract market or derivatives transaction execution facility, or a significant price discovery contract or contracts trading on or subject to the rules of an electronic trading facility, so as to permit market participants to effectively arbitrage between the markets by simultaneously maintaining positions or executing trades in the contracts on a frequent and recurring basis.*

(1) Arbitrage contracts are those contracts that can be combined with other contracts to exploit expected economic relationships in anticipation of a profit. In assessing whether a contract can be incorporated into an arbitrage strategy, the Commission will weigh the terms and conditions of a contract in comparison to contracts that potentially could be used in an arbitrage strategy; will consult with industry or other sources regarding a contract's viability in an arbitrage strategy; and will rely on direct observation confirming the use of a contract in arbitrage strategies.

(2) As with linked contracts, the mere fact that a contract could be employed in an arbitrage strategy will not be sufficient to make a determination that a contract is a significant price discovery contract. In addition, the level of liquidity will be considered. To assess whether designation as a significant price discovery contract is warranted, the Commission will examine the relationship between transaction prices of an arbitrage contract and the prices of the contract(s) to which it is related. The Commission believes that where material liquidity exists, prices for the arbitrage contract would be observed to move substantially in conjunction with the prices of the related contract(s) to which it is economically linked. Where such price characteristics are observed on an ongoing basis, it is likely that the linked contract performs a significant price discovery function.

(3) The Commission will apply the same threshold liquidity and price relationship standards for arbitrage contracts as it does for linked contracts. That is, the Commission will view the average of 5 trades per day or more threshold as the level of activity that would potentially meet the material volume criterion. With respect to prices, the Commission will consider an arbitrage

contract potentially to be a significant price discovery contract if, over the most recent quarter, greater than 95 percent of the closing or settlement prices of the contract, which have been calculated using transaction prices, fall within 2.5 percent of the closing or settlement price of the contract or contracts to which it could be arbitrated.

(D) *MATERIAL PRICE REFERENCE*—*The extent to which, on a frequent and recurring basis, bids, offers or transactions in a commodity are directly based on, or are determined by referencing, the prices generated by agreements, contracts or transactions being traded or executed on the electronic trading facility.*

(1) The Commission will rely on one of two sources of evidence—direct or indirect—to determine that the price of a contract was being used as a material price reference and, therefore, serving a significant price discovery function. The primary source of direct evidence is that cash market bids, offers or transactions are directly based on, or quoted at a differential to, the prices generated on the market on a frequent and recurring basis. The Commission expects that normally only contracts with material liquidity will be referenced by the cash market; however, the Commission notes that it may be possible for a contract to have very low liquidity and yet still be used as a price reference. In such cases, the simple fact that participants in the underlying cash market broadly have elected to use the contract price as a price reference would be a strong indicator that the contract is a significant price discovery contract.

(2) In evaluating a contract's price discovery role as a directly referenced price source, the Commission will perform an analysis to determine whether cash market participants are quoting bid or offer prices or entering into transactions at prices that are set either explicitly or implicitly at a differential to prices established for the contract. Cash market prices are set explicitly at a differential to the section 2(h)(3) contract when, for instance, they are quoted in dollars and cents above or below the reference contract's price. Cash market prices are set implicitly at a differential to a section 2(h)(3) contract when, for instance, they are arrived at after adding to, or subtracting from the section 2(h)(3) contract, but then quoted or reported at a flat price. The Commission will also consider whether cash market entities are quoting cash prices based on a section 2(h)(3) contract on a frequent and recurring basis.

(3) The second source of evidence is that the price of the contract is being routinely disseminated in widely distributed industry publications—or offered by the ECM itself for some form of remuneration—and consulted on a frequent and recurring basis by industry participants in pricing cash market transactions. As with contract prices that are directly incorporated into cash market prices, the Commission assumes that industry publications choose to publish prices because of the value they transfer to industry participants for the purpose of formulating prices in the cash market.

(4) In applying this criterion, consideration will be given to whether prices established

by a section 2(h)(3) contract are reported in a widely distributed industry publication. In making this determination, the Commission will consider the reputation of the publication within the industry, how frequently it is published, and whether the information contained in the publication is routinely consulted by industry participants in pricing cash market transactions.

(5) Under a Material Price Reference analysis, the Commission expects that material liquidity in the contract likely will be the primary motivation for a publisher to publish particular prices. In other words, the fact that the price of a contract is being used as a reference by industry participants suggests, *prima facie*, that the contract performs a significant price discovery function. But the Commission recognizes that trading levels could nonetheless be low for the contract while still serving a significant price discovery function and that evidence of routine publication and consultation by industry participants may be sufficient to establish the contract as a significant price discovery contract. On the other hand, while cash market participants may regularly refer to published prices of a particular contract when establishing cash market prices, it may be the case that the contract itself is a niche market for a specialized grade of the commodity or for delivery at a minor geographic location. In such cases, the Commission will look to such measures as trading volume, open interest, and the significance of the underlying cash market to make a determination that a contract is functioning as a significant price discovery contract. If an examination of trading in the contract were to reveal that true price discovery was occurring in other more broadly defined contracts and that this contract was itself simply reflective of those broader contracts, it is less likely the Commission will deem the contract a significant price discovery contract.

(6) Because price referencing normally occurs out of the view of the electronic trading facility, the Commission may have difficulty ascertaining the extent to which cash market participants actually reference or consult a contract's price when transacting. The Commission expects, however, that as a contract begins to be relied upon to set a reference price, market participants will be increasingly willing to purchase price information. To the extent, then, that an electronic trading facility begins to sell its price information regarding a contract to market participants or industry publications, the contract will meet a threshold standard to indicate that the contract potentially is a significant price discovery contract.

32. Part 36 is amended by adding a new Appendix B to read as follows:

**Appendix B to Part 36—Guidance On, and Acceptable Practices in, Compliance With Core Principles**

1. This Appendix provides guidance on complying with the core principles under section 2(h)(7)(C) of the Act and this part, both initially and on an ongoing basis. The guidance is provided in paragraph (a) following each core principle and can be

used to demonstrate to the Commission core principle compliance under § 36.3(c)(4). The guidance for each core principle is illustrative only of the types of matters an electronic trading facility may address, as applicable, and is not intended to be used as a mandatory checklist. Addressing the issues and questions set forth in this guidance will help the Commission in its consideration of whether the electronic trading facility is in compliance with the core principles. A submission pursuant to § 36.3(c)(4) should include an explanation or other form of documentation demonstrating that the electronic trading facility complies with the core principles.

2. Acceptable practices meeting selected requirements of the core principles are set forth in paragraph (b) following each core principle. Electronic trading facilities on which significant price discovery contracts are traded or executed that follow the specific practices outlined under paragraph (b) for any core principle in this appendix will meet the selected requirements of the applicable core principle. Paragraph (b) is for illustrative purposes only, and does not state the exclusive means for satisfying a core principle.

*CORE PRINCIPLE I OF SECTION 2(h)(7)(C)—CONTRACTS NOT READILY SUSCEPTIBLE TO MANIPULATION. The electronic trading facility shall list only significant price discovery contracts that are not readily susceptible to manipulation.*

(a) *Guidance.* Upon determination by the Commission that a contract listed for trading on an electronic trading facility is a significant price discovery contract, the electronic trading facility must self-certify the terms and conditions of the significant price discovery contract under § 36.3(c)(4) within 90 calendar days of the date of the Commission's order, if the contract is the electronic trading facility's first significant price discovery contract; or 15 days from the date of the Commission's order if the contract is not the electronic trading facility's first significant price discovery contract. Once the Commission determines that a contract performs a significant price discovery function, subsequent rule changes must be self-certified to the Commission by the electronic trading facility pursuant to § 40.6 of this chapter.

(b) *Acceptable practices.* Guideline No. 1, 17 CFR part 40, Appendix A may be used as guidance in meeting this core principle for significant price discovery contracts.

*CORE PRINCIPLE II OF SECTION 2(h)(7)(C)—MONITORING OF TRADING. The electronic trading facility shall monitor trading in significant price discovery contracts to prevent market manipulation, price distortion, and disruptions of the delivery of cash-settlement process through market surveillance, compliance and disciplinary practices and procedures, including methods for conducting real-time monitoring of trading and comprehensive and accurate trade reconstructions.*

(a) *Guidance.* An electronic trading facility on which significant price discovery contracts are traded or executed should, with respect to those contracts, demonstrate a capacity to prevent market manipulation and

have trading and participation rules to detect and deter abuses. The facility should seek to prevent market manipulation and other trading abuses through a dedicated regulatory department or by delegation of that function to an appropriate third party. An electronic trading facility also should have the authority to intervene as necessary to maintain an orderly market.

(b) *Acceptable practices.*

(1) *An acceptable trade monitoring program.* An acceptable trade monitoring program should facilitate, on both a routine and non-routine basis, arrangements and resources to detect and deter abuses through direct surveillance of each significant price discovery contract. Direct surveillance of each significant price discovery contract will generally involve the collection of various market data, including information on participants' market activity. Those data should be evaluated on an ongoing basis in order to make an appropriate regulatory response to potential market disruptions or abusive practices. For contracts with a substantial number of participants, an effective surveillance program should employ a much more comprehensive large trader reporting system.

(2) *Authority to collect information and documents.* The electronic trading facility should have the authority to collect information and documents in order to reconstruct trading for appropriate market analysis. Appropriate market analysis should enable the electronic trading facility to assess whether each significant price discovery contract is responding to the forces of supply and demand. Appropriate data usually include various fundamental data about the underlying commodity, its supply, its demand, and its movement through market channels. Especially important are data related to the size and ownership of deliverable supplies—the existing supply and the future or potential supply—and to the pricing of the deliverable commodity relative to the futures price and relative to similar, but non-deliverable, kinds of the commodity. For cash-settled contracts, it is more appropriate to pay attention to the availability and pricing of the commodity making up the index to which the contract will be settled, as well as monitoring the continued suitability of the methodology for deriving the index.

(3) *Ability to assess participants' market activity and power.* To assess participants' activity and potential power in a market, electronic trading facilities, with respect to significant price discovery contracts, at a minimum should have routine access to the positions and trading of its participants and, if applicable, should provide for such access through its agreements with its third-party provider of clearing services.

**CORE PRINCIPLE III OF SECTION 2(h)(7)(C)—ABILITY TO OBTAIN INFORMATION.** *The electronic trading facility shall establish and enforce rules that allow the electronic trading facility to obtain any necessary information to perform any of the functions described in this subparagraph, provide the information to the Commission upon request, and have the capacity to carry out such international information-sharing agreements as the Commission may require.*

(a) *Guidance.* An electronic trading facility on which significant price discovery contracts are traded or executed should, with respect to those contracts, have the ability and authority to collect information and documents on both a routine and non-routine basis, including the examination of books and records kept by participants. This includes having arrangements and resources for recording full data entry and trade details and safely storing audit trail data. An electronic trading facility should have systems sufficient to enable it to use the information for purposes of assisting in the prevention of participant and market abuses through reconstruction of trading and providing evidence of any violations of the electronic trading facility's rules.

(b) *Acceptable practices.*

(1) The goal of an audit trail is to detect and deter market abuse. An effective contract audit trail should capture and retain sufficient trade-related information to permit electronic trading facility staff to detect trading abuses and to reconstruct all transactions within a reasonable period of time. An audit trail should include specialized electronic surveillance programs that identify potentially abusive trades and trade patterns. An acceptable audit trail must be able to track an order from time of entry into the trading system through its fill. The electronic trading facility must create and maintain an electronic transaction history database that contains information with respect to transactions executed on each significant price discovery contract.

(2) An acceptable audit trail should include the following: original source documents, transaction history, electronic analysis capability, and safe storage capability. An acceptable audit trail system would satisfy the following practices.

(i) *Original source documents.* Original source documents include unalterable, sequentially identified records on which trade execution information is originally recorded. For each order (whether filled, unfilled or cancelled, each of which should be retained or electronically captured), such records reflect the terms of the order, an account identifier that relates back to the account(s) owner(s), and the time of order entry.

(ii) *Transaction history.* A transaction history consists of an electronic history of each transaction, including:

(A) All the data that are input into the trade entry or matching system for the transaction to match and clear;

(B) Timing and sequencing data adequate to reconstruct trading; and

(C) The identification of each account to which fills are allocated.

(iii) *Electronic analysis capability.* An electronic analysis capability that permits sorting and presenting data included in the transaction history so as to reconstruct trading and to identify possible trading violations with respect to market abuse.

(iv) *Safe storage capability.* Safe storage capability provides for a method of storing the data included in the transaction history in a manner that protects the data from unauthorized alteration, as well as from accidental erasure or other loss. Data should

be retained in the form and manner specified by the Commission or, where no acceptable manner of retention is specified, in accordance with the recordkeeping standards of Commission regulation 1.31.

(3) Arrangements and resources for the disclosure of the obtained information and documents to the Commission upon request. To satisfy section 2(h)(7)(C)(III)(bb), the electronic trading facility should maintain records of all information and documents related to each significant price discovery contract in a form and manner acceptable to the Commission. Where no acceptable manner of maintenance is specified, records should be maintained in accordance with the recordkeeping standards of Commission regulation 1.31.

(4) The capacity to carry out appropriate information-sharing agreements as the Commission may require. Appropriate information-sharing agreements could be established with other markets or the Commission can act in conjunction with the electronic trading facility to carry out such information sharing.

**CORE PRINCIPLE IV OF SECTION 2(h)(7)(C)—POSITION LIMITATIONS OR ACCOUNTABILITY.** *The electronic trading facility shall adopt, where necessary and appropriate, position limitations or position accountability for speculators in significant price discovery contracts, taking into account positions in other agreements, contracts and transactions that are treated by a derivatives clearing organization, whether registered or not registered, as fungible with such significant price discovery contracts to reduce the potential threat of market manipulation or congestion, especially during trading in the delivery month.*

(a) *Guidance.* [Reserved]

(b) *Acceptable practices.*

(1) *Introduction.* In order to diminish potential problems arising from excessively large speculative positions, and to facilitate orderly liquidation of expiring contracts, an electronic trading facility relying on the exemption in section 2(h)(3) should adopt rules that set position limits or accountability levels on traders' cleared positions in significant price discovery contracts. These position limit rules specifically may exempt bona fide hedging; permit other exemptions; or set limits differently by market, delivery month or time period. For the purpose of evaluating a significant price discovery contract's speculative-limit program for cleared positions, the Commission will consider the specified position limits or accountability levels, aggregation policies, types of exemptions allowed, methods for monitoring compliance with the specified limits or levels, and procedures for dealing with violations.

(2) *Accounting for cleared and uncleared trades.*

(i) Speculative-limit levels typically should be set in terms of a trader's combined position involving cleared trades in a significant price discovery contract, plus positions in agreements, contracts and transactions that are treated by a derivatives clearing organization, whether registered or not registered, as fungible with such significant price discovery contract. (This



circumstance typically exists where an exempt commercial market lists a particular contract for trading but also allows for positions in that contract to be cleared together with positions established through bilateral or off-exchange transactions, such as block trades, in the same contract.

Essentially, both the on-facility and off-facility transactions are considered fungible with each other.) In this connection, the electronic trading facility should make arrangements to ensure that it is able to ascertain accurate position data for the market.

(ii) For significant price discovery contracts that may be traded on either a cleared or an uncleared basis, the electronic trading facility should apply position limits to cleared transactions in the contract. For those transactions in the contract that are not cleared, the electronic trading facility should establish accountability procedures for monitoring traders' overall positions and take that information into account when ascertaining whether an individual trader's overall position poses a threat to the market.

(3) *Limitations on spot-month positions.* Spot-month limits should be adopted for significant price discovery contracts to minimize the susceptibility of the market to manipulation or price distortions, including squeezes and corners or other abusive trading practices.

(i) *Contracts economically equivalent to an existing contract.* An electronic trading facility that lists a significant price discovery contract that is economically-equivalent to another significant price discovery contract or to a contract traded on a designated contract market or derivatives transaction execution facility should set the spot-month limit for its significant price discovery contract at the same level as that specified for the economically-equivalent contract.

(ii) *Contracts that are not economically equivalent to an existing contract.* There may not be an economically-equivalent significant price discovery contract or economically equivalent contract traded on a designated contract market or derivatives transaction execution facility. In this case, the spot-month speculative position limit should be established in the following manner. The spot-month limit for a physical delivery market should be based upon an analysis of deliverable supplies and the history of spot-month liquidations. The spot-month limit for a physical-delivery market is appropriately set at no more than 25 percent of the estimated deliverable supply. In the case where a significant price discovery contract has a cash settlement provision, the spot-month limit should be set at a level that minimizes the potential for price manipulation or distortion in the significant price discovery contract itself; in related futures and options contracts traded on a designated contract market or derivatives transaction execution facility; in other significant price discovery contracts; in other fungible agreements, contracts and transactions; and in the underlying commodity.

(4) *Position accountability for non-spot-month positions.* The electronic trading facility should establish for its significant

price discovery contracts non-spot individual month position accountability levels and all-months-combined position accountability levels. An electronic trading facility may establish non-spot individual month position limits and all-months-combined position limits for its significant price discovery contracts in lieu of position accountability levels.

(i) *Definition.* Position accountability provisions provide a means for an exchange to monitor traders' positions that may threaten orderly trading. An acceptable accountability provision sets target accountability threshold levels that may be exceeded, but once a trader breaches such accountability levels, the electronic trading facility should initiate an investigation to determine whether the individual's trading activity is justified and is not intended to manipulate the market. As part of its investigation, the electronic trading facility should inquire about the trader's rationale for holding a position in excess of the accountability levels. An acceptable accountability provision should provide the electronic trading facility with the authority to order the trader not to further increase positions. If a trader fails to comply with a request for information about positions held, provides information that does not sufficiently justify the position, or continues to increase contract positions after a request not to do so is issued by the facility, then the accountability provision should enable the electronic trading facility to require the trader to reduce positions.

(ii) *Contracts economically equivalent to an existing contract.* When an electronic trading facility lists a significant price discovery contract that is economically equivalent to another significant price discovery contract or to a contract traded on a designated contract market or derivatives transaction execution facility, the electronic trading facility should set the non-spot individual month position accountability level and all-months-combined position accountability level for its significant price discovery contract at the same levels, or lower, as those specified for the economically-equivalent contract.

(iii) *Contracts that are not economically equivalent to an existing contract.* For significant price discovery contracts that are not economically equivalent to an existing contract, the trading facility shall adopt non-spot individual month and all-months-combined position accountability levels that are no greater than 10 percent of the average combined futures and delta-adjusted option month-end open interest for the most recent calendar year. For electronic trading facilities that choose to adopt non-spot individual month and all-months-combined position limits in lieu of position accountability levels for their significant price discovery contracts, the limits should be set in the same manner as the accountability levels.

(iv) *Contracts economically equivalent to an existing contract with position limits.* If a significant price discovery contract is economically equivalent to another significant price discovery contract or to a contract traded on a designated contract market or derivatives transaction execution

facility that has adopted non-spot or all-months-combined position limits, the electronic trading facility should set non-spot month position limits and all-months-combined position limits for its significant price discovery contract at the same (or lower) levels as those specified for the economically-equivalent contract.

(5) *Provisions for uncleared contracts.* If an electronic trading facility offers a significant price discovery contract that is exclusively uncleared, or one that may be either cleared by a derivatives clearing organization or uncleared at the discretion of the trader, the trading facility should establish for the uncleared trades a spot-month volume accountability level equal to the spot-month speculative position limit. In this regard, the electronic trading facility should keep track of each trader's uncleared transactions in a significant price discovery contract on a net basis. (For the purpose of netting uncleared transactions, long and short uncleared transactions are only offset if they are conducted with the same counterparty.) If a particular trader's net volume of uncleared transactions exceeds the specified spot-month volume accountability level, the electronic trading facility should conduct an investigation to determine whether the trader's trading activity is warranted and is not intended to manipulate the market.

(6) *Account aggregation.* An electronic trading facility should have aggregation rules for significant price discovery contracts that apply to accounts under common control, those with common ownership, *i.e.*, where there is a ten percent or greater financial interest, and those traded according to an express or implied agreement. Such aggregation rules should apply to cleared transactions with respect to applicable speculative position limits, as well as to uncleared transactions with respect to applicable spot-month volume accountability levels. An electronic trading facility will be permitted to set more stringent aggregation policies. An electronic trading facility may grant exemptions to its price discovery contracts' position limits for bona fide hedging (as defined in § 1.3(z) of this chapter) and may grant exemptions for reduced risk positions, such as spreads, straddles and arbitrage positions.

(7) *Implementation deadlines.* An electronic trading facility with a significant price discovery contract is required to comply with Core Principle IV as set forth in section 2(h)(7)(C) of the Act within 90 calendar days of the date of the Commission's order determining that the contract performs a significant price discovery function if such contract is the electronic trading facility's first significant price discovery contract, or within 15 days of the date of the Commission's order if such contract is not the electronic trading facility's first significant price discovery contract. For the purpose of applying limits on speculative positions in newly-determined significant price discovery contracts, the Commission will permit a grace period following issuance of its order for traders with cleared positions in such contracts to become compliant with applicable position limit rules. Traders who hold cleared positions on a net basis in the

electronic trading facility's significant price discovery contract must be at or below the specified position limit level no later than 90 calendar days from the date of the electronic trading facility's implementation of position limit rules, unless a hedge exemption is granted by the electronic trading facility. This grace period applies to both initial and subsequent price discovery contracts. Electronic trading facilities should notify traders of this requirement promptly upon implementation of such rules.

(8) *Enforcement provisions.* The electronic trading facility should have appropriate procedures in place to monitor its position limit and accountability provisions and to address violations.

(i) An electronic trading facility with significant price discovery contracts should use an automated means of detecting traders' violations of speculative limits or exemptions, particularly if the significant price discovery contracts have large numbers of traders. An electronic trading facility should monitor the continuing appropriateness of approved exemptions by periodically reviewing each trader's basis for exemption or requiring a reapplication. An automated system also should be used to determine whether a trader has exceeded applicable non-spot individual month position accountability levels, all-months-combined position accountability levels, and spot-month volume accountability levels.

(ii) An electronic trading facility should establish a program for effective enforcement of position limits for significant price discovery contracts. Electronic trading facilities should use a large trader reporting system to monitor and enforce daily compliance with position limit rules. The Commission notes that an electronic trading facility may allow traders to periodically apply to the electronic trading facility for an exemption and, if appropriate, be granted a position level higher than the applicable speculative limit. The electronic trading facility should establish a program to monitor approved exemptions from the limits. The position levels granted under such hedge exemptions generally should be based upon the trader's commercial activity in related markets including, but not limited to, positions held in related futures and options contracts listed for trading on designated contract markets, fungible agreements, contracts and transactions, as determined by either a registered or unregistered derivatives clearing organization. Electronic trading facilities may allow a brief grace period where a qualifying trader may exceed speculative limits or an existing exemption level pending the submission and approval of appropriate justification. An electronic trading facility should consider whether it wants to restrict exemptions during the last several days of trading in a delivery month. Acceptable procedures for obtaining and granting exemptions include a requirement that the electronic trading facility approve a specific maximum higher level.

(iii) An acceptable speculative limit program should have specific policies for taking regulatory action once a violation of a position limit or exemption is detected. The electronic trading facility policies should consider appropriate actions.

(9) *Violation of Commission rules.* A violation of position limits for significant price discovery contracts that have been self-certified by an electronic trading facility also a violation of section 4a(e) of the Act.

**CORE PRINCIPLE V OF SECTION 2(h)(7)(C)—EMERGENCY AUTHORITY—***The electronic trading facility shall adopt rules to provide for the exercise of emergency authority, in consultation or cooperation with the Commission, where necessary and appropriate, including the authority to liquidate open positions in significant price discovery contracts and to suspend or curtail trading in a significant price discovery contract.*

(a) *Guidance.* An electronic trading facility on which significant price discovery contracts are traded should have clear procedures and guidelines for decision-making regarding emergency intervention in the market, including procedures and guidelines to avoid conflicts of interest while carrying out such decision-making. An electronic trading facility on which significant price discovery contracts are executed or traded should also have the authority to intervene as necessary to maintain markets with fair and orderly trading as well as procedures for carrying out the intervention. Procedures and guidelines should include notifying the Commission of the exercise of the electronic trading facility's regulatory emergency authority, explaining how conflicts of interest are minimized, and documenting the electronic trading facility's decision-making process and the reasons for using its emergency action authority. Information on steps taken under such procedures should be included in a submission of a certified rule and any related submissions for rule approval pursuant to part 40 of this chapter, when carried out pursuant to an electronic trading facility's emergency authority. To address perceived market threats, the electronic trading facility on which significant price discovery contracts are executed or traded should, among other things, be able to impose position limits in the delivery month, impose or modify price limits, modify circuit breakers, call for additional margin either from market participants or clearing members (for contracts that are cleared through a clearinghouse), order the liquidation or transfer of open positions, order the fixing of a settlement price, order a reduction in positions, extend or shorten the expiration date or the trading hours, suspend or curtail trading on the electronic trading facility, order the transfer of contracts and the margin for such contracts from one market participant to another, or alter the delivery terms or conditions or, if applicable, should provide for such actions through its agreements with its third-party provider of clearing services.

(b) *Acceptable practices.* [Reserved]

**CORE PRINCIPLE VI OF SECTION 2(h)(7)(C)—DAILY PUBLICATION OF TRADING INFORMATION.** *The electronic trading facility shall make public daily information on price, trading volume, and other trading data to the extent appropriate for significant price discovery contracts.*

(a) *Guidance.* An electronic trading facility, with respect to significant price discovery

contracts, should provide to the public information regarding settlement prices, price range, volume, open interest, and other related market information for all applicable contracts as determined by the Commission on a fair, equitable and timely basis. Provision of information for any applicable contract can be through such means as provision of the information to a financial information service or by timely placement of the information on the electronic trading facility's public Web site.

(b) *Acceptable practices.* Compliance with § 16.01 of this chapter, which is mandatory, is an acceptable practice and satisfies the requirements of under Core Principle VI.

**CORE PRINCIPLE VII OF SECTION 2(h)(7)(C)—COMPLIANCE WITH RULES.** *The electronic trading facility shall monitor and enforce compliance with the rules of the electronic trading facility, including the terms and conditions of any contracts to be traded and any limitations on access to the electronic trading facility.*

(a) *Guidance.*

(1) An electronic trading facility on which significant price discovery contracts are executed or traded should have appropriate arrangements and resources for effective trade practice surveillance programs, with the authority to collect information and documents on both a routine and non-routine basis, including the examination of books and records kept by its market participants. The arrangements and resources should facilitate the direct supervision of the market and the analysis of data collected. Trade practice surveillance programs may be carried out by the electronic trading facility itself or through delegation or contracting-out to a third party. If the electronic trading facility on which significant price discovery contracts are executed or traded delegates or contracts-out the trade practice surveillance responsibility to a third party, such third party should have the capacity and authority to carry out such programs, and the electronic trading facility should retain appropriate supervisory authority over the third party.

(2) An electronic trading facility on which significant price discovery contracts are executed or traded should have arrangements, resources and authority for effective rule enforcement. The Commission believes that this should include the authority and ability to discipline and limit or suspend the activities of a market participant as well as the authority and ability to terminate the activities of a market participant pursuant to clear and fair standards. The electronic trading facility can satisfy this criterion for market participants by expelling or denying such person's future access upon a determination that such a person has violated the electronic trading facility's rules.

(b) *Acceptable practices.* An acceptable trade practice surveillance program generally would include:

(1) Maintenance of data reflecting the details of each transaction executed on the electronic trading facility;

(2) Electronic analysis of this data routinely to detect potential trading violations;

(3) Appropriate and thorough investigative analysis of these and other potential trading violations brought to the electronic trading facility's attention; and

(4) Prompt and effective disciplinary action for any violation that is found to have been committed. The Commission believes that the latter element should include the authority and ability to discipline and limit or suspend the activities of a market participant pursuant to clear and fair standards that are available to market participants. See, e.g., 17 CFR part 8.

**CORE PRINCIPLE VIII OF SECTION 2(h)(7)(C)—CONFLICTS OF INTEREST.** *The electronic trading facility on which significant price discovery contracts are executed or traded shall establish and enforce rules to minimize conflicts of interest in the decision-making process of the electronic trading facility and establish a process for resolving such conflicts of interest.*

(a) *Guidance.*

(1) The means to address conflicts of interest in the decision-making of an electronic trading facility on which significant price discovery contracts are executed or traded should include methods to ascertain the presence of conflicts of interest and to make decisions in the event of such a conflict. In addition, the Commission believes that the electronic trading facility on which significant price discovery contracts are executed or traded should provide for appropriate limitations on the use or disclosure of material non-public information gained through the performance of official duties by board members, committee members and electronic trading facility employees or gained through an ownership interest in the electronic trading facility or its parent organization(s).

(2) All electronic trading facilities on which significant price discovery contracts are traded bear special responsibility to regulate effectively, impartially, and with due consideration of the public interest, as provided in section 3 of the Act. Under Core Principle VIII, they are also required to minimize conflicts of interest in their decision-making processes. To comply with this core principle, electronic trading facilities on which significant price discovery contracts are traded should be particularly vigilant for such conflicts between and among any of their self-regulatory responsibilities, their commercial interests, and the several interests of their management, members, owners, market participants, other industry participants and other constituencies.

(b) *Acceptable practices.* [Reserved]

**CORE PRINCIPLE IX OF SECTION 2(h)(7)(C)—ANTITRUST CONSIDERATIONS.** *Unless necessary or appropriate to achieve the purposes of this Act, the electronic trading facility, with respect to any significant price discovery contracts, shall endeavor to avoid adopting any rules or taking any actions that result in any unreasonable restraints of trade or imposing any material anticompetitive burden on trading on the electronic trading facility.*

(a) *Guidance.* An electronic trading facility, with respect to a significant price discovery

contract, may at any time request that the Commission consider under the provisions of section 15(b) of the Act any of the electronic trading facility's rules, which may be trading protocols or policies, operational rules, or terms or conditions of any significant price discovery contract. The Commission intends to apply section 15(b) of the Act to its consideration of issues under this core principle in a manner consistent with that previously applied to contract markets.

(b) *Acceptable practices.* [Reserved]

**PART 40—PROVISIONS COMMON TO REGISTERED ENTITIES**

33. The authority citation for part 40 is revised to read as follows:

**Authority:** 7 U.S.C. 1a, 2, 5, 6, 6c, 7, 7a, 8 and 12a, as amended by Title XIII of the Food, Conservation and Energy Act of 2008, Pub. L. No. 110–246, 122 Stat. 1624 (June 18, 2008).

34. Revise the heading of part 40 as set forth above.

35. Amend § 40.1 as follows:

A. Remove the term “registered entity” and add in its place the term “contract market, derivatives transaction execution facility or derivatives clearing organization” in paragraphs (b)(2), (b)(3), and (f)(2); and

B. Remove the term “contract market, derivatives transaction execution facility or derivatives clearing organization” and add in its place the term “registered entity” in paragraph (h).

36. Amend § 40.2 as follows:

A. Remove the term “registered entity” and add in its place “contract market, derivatives transaction execution facility on which significant price discovery contracts are traded or executed” in paragraph (a);

B. Remove the term “registered entity” and add in its place “contract market, derivatives transaction execution facility or derivatives clearing organization” in paragraphs (a)(1) and (a)(3)(iv); and

C. Revise paragraph (b) to read as follows:

**§ 40.2 Listing and accepting products for trading or clearing by certification.**

\* \* \* \* \*

(b) A registered entity shall provide, if requested by Commission staff, additional evidence, information or data relating to whether any contract meets, initially or on a continuing basis, any of the requirements of the Act or Commission regulations or policies thereunder which may be beneficial to the Commission in conducting a due diligence assessment of the product and the entity's compliance with these requirements.

\* \* \* \* \*

37. In § 40.3, remove the term “registered entity” and add in its place the term “designated contract market or registered derivatives transaction execution facility” in paragraphs (a)(1), (c)(1), (c)(2), and (e)(2).

38. In § 40.4, remove the term “registered entity” and add in its place the term “designated contract market” in paragraph (b)(9)(ii).

39. In § 40.6, revise paragraphs (a)(2), (c)(3)(ii)(G), and (c)(3)(ii)(H) to read as follows:

**§ 40.6 Self-certification of rules.**

(a) \* \* \*

(2) The registered entity has filed its submission electronically in a format specified by the Secretary of the Commission with the Secretary of the Commission at *submissions@cftc.gov*, the relevant branch chief at the regional office having local jurisdiction over the registered entity, and, for filings submitted by a designated contract market, registered derivatives transaction execution facility, or electronic trading facility on which significant price discovery contracts are traded or executed, the Division of Market Oversight at *DMOSubmissions@cftc.gov*, and the Commission has received the submission at its headquarters by the open of business on the business day preceding implementation of the rule; *provided, however*, rules or rule amendments implemented under procedures of the governing board to respond to an emergency as defined in § 40.1, shall, if practicable, be filed with the Commission prior to the implementation or, if not practicable, be filed with the Commission at the earliest possible time after implementation, but in no event more than twenty-four hours after implementation; and

\* \* \* \* \*

(c) \* \* \*

(3) \* \* \*

(ii) \* \* \*

(G) *Option contract terms.* For registered entities that are in compliance with the daily reporting requirements of § 16.01 of this chapter, changes to option contract rules relating to the strike price listing procedures, strike price intervals, and the listing of strike prices on a discretionary basis.

(H) *Trading months.* For registered entities that are in compliance with the daily reporting requirements of § 16.01 of this chapter, the initial listing of trading months which are within the currently established cycle of trading months.

40. In § 40.7, remove the term “designated contract market, registered derivatives transaction execution

facility or registered derivatives clearing organization” and add in its place the term “registered entity” in paragraph (b) introductory text.

41. In § 40.8, revise paragraph (a), redesignate paragraph (b) as paragraph (c), and add new paragraph (b) to read as follows:

**§ 40.8 Availability of public information.**

(a) The following sections of all applications to become a designated contract market, derivatives execution transaction facility or designated clearing organization will be public: transmittal letter, proposed rules, the applicant’s regulatory compliance chart, documents establishing the applicant’s legal status, documents setting forth the applicant’s governance structure, and any other part of the application not covered by a request for confidential treatment.

(b) The following submissions required by § 36.3(c)(4) by an electronic trading facility on which significant price discovery contracts are traded or executed will be public: rulebook, the facility’s regulatory compliance chart, documents establishing the facility’s legal status, documents setting forth the

facility’s governance structure, and any other parts of the submissions not covered by a request for confidential treatment.

\* \* \* \* \*

42. Revise Appendix D to part 40 to read as follows:

**Appendix D to Part 40—Submission Cover Sheet and Instructions**

A properly completed submission cover sheet must accompany all rule submissions submitted electronically by a registered entity to the Secretary of the Commodity Futures Trading Commission, at *submissions@cftc.gov* in a format specified by the Secretary of the Commission. Each submission should include the following:

1. *Identifier Code (optional)*—If applicable, the exchange or clearing organization Identifier Code at the top of the cover sheet. Such codes are commonly generated by the exchanges or clearing organizations to provide an identifier that is unique to each filing (e.g., NYMEX Submission 03–116).
2. *Date*—The date of the filing.
3. *Organization*—The name of the organization filing the submission (e.g., CBOT).
4. *Filing as a*—Check the appropriate box for a designated contract market (DCM), derivatives clearing organization (DCO), derivatives transaction execution facility

(DTEF), or electronic trading facility with a significant price discovery contract (ECM–SPDC).

5. *Type of Filing*—Indicate whether the filing is a rule amendment or new product and the applicable category under that heading.

6. *Rule Numbers*—For rule filings only, identify rule number(s) being adopted or modified in the case of rule amendment filings.

7. *Description*—For rule or rule amendment filings only, enter a brief description of the new rule or rule amendment. This narrative should describe the substance of the submission with enough specificity to characterize all essential aspects of the filing.

8. *Other Requirements*—Comply with all filing requirements for the underlying proposed rule or rule amendment. The filing of the submission cover sheet does not obviate the responsibility to comply with any applicable filing requirement (e.g., rules submitted for Commission approval under § 40.5 must be accompanied by an explanation of the purpose and effect of the proposed rule along with a description of any substantive opposing views).

A sample of the required submission cover sheet follows.

**BILLING CODE 6351–01–P**

## SUBMISSION COVER SHEET

Exchange Identifier Code (optional)

Date:

**IMPORTANT:**

**CHECK BOX IF CONFIDENTIAL TREATMENT IS REQUESTED.**

**ORGANIZATION**

**FILING AS A:**  DCM  DCO  DTEF  ECM/SPDC

**TYPE OF FILING**

- **Rule Amendments**

- Self-Certification Under Reg. 40.6(a) or 41.24
- Commission Approval Requested Under Reg. 40.5 or 40.4 (a)
- Notification of Rule Amendment Under Reg. 40.6(c)
- Non-Material Agricultural Rule Change Determination Under Reg. 40.4(b)

- **New Products**

- Self-Certification Under Reg. 40.2 or 41.23
- Commission Approval Requested Under Reg. 40.3

**RULE NUMBERS**

**DESCRIPTION (Rule Amendments Only)**

Issued in Washington, DC, on December 2, 2008, by the Commission.

**David Stawick,**

*Secretary of the Commission.*

[FR Doc. E8-28867 Filed 12-11-08; 8:45 am]

**BILLING CODE 6351-01-C**